Jurisdictional Statement

81-1002

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Case No.

In the Supreme Court of the United States

October Term, 1981

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

Appellant,

vs.

OFFICE OF CONSUMERS' COUNSEL, SENIOR CITIZENS COALITION, GREATER CLEVELAND WELFARE RIGHTS ORGANIZATION, INC., WESTERN RESERVE ALLIANCE, NORTH SHORE ALERT, CLEVELAND CHAPTER OF OHIOANS FOR UTILITY REFORM,

and

THE PUBLIC UTILITIES COMMISSION OF OHIO,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF OHIO

JURISDICTIONAL STATEMENT

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QUESTIONS PRESENTED

1. May the State of Ohio, by statute, constitutionally require a public utility to invest its capital to provide adequate service for the convenience of the public in the future and simultaneously prohibit, by statute, that utility from recovering through rates such capital when prudently invested?

2. May the State of Ohio, by statute, constitutionally prohibit a public utility from recovering through rates its capital, prudently invested for the convenience of the public, where the undisputed facts show that the utility, and its investors, have never been compensated through the authorized or achieved rate of return for the risk of exclusion of such costs from rates?

TABLE OF CONTENTS

	Page
Questions Presented	i
Table of Authorities	iv
Reports of Opinions Below	1
Grounds For Jurisdiction	1
Constitutional Provisions, Statutes, and Regulations Involved	2
Statement of the Case	3
A. The course of proceedings and their disposition in the courts below	3
B. The facts material to the questions presented	5
C. The decision of the Supreme Court of Ohio	9
D. The stage at which the question sought to be reviewed was raised below	10
Reasons Requiring Plenary Consideration	12
I. OHIO REVISED CODE § 4905.22 AND § 4909.15(A)(4), AS CONSTRUED BY THE SUPREME COURT OF OHIO, DIRECTLY CONFLICT WITH THE PROSCRIPTION OF THE FIFTH AND FOURTEENTH AMENDMENTS TO THE CONSTITUTION OF THE UNITED STATES PROHIBITING CONFISCATION OF PRIVATE PROPERTY WITHOUT DUE PROCESS OF LAW	12
II. OHIO REVISED CODE § 4905.22 AND § 4909.15(A)(4), AS CONSTRUED BELOW, DIRECTLY CONFLICT WITH THIS COURT'S DECISION IN *FEDERAL POWER COMMISSION V. HOPE NATURAL GAS CO.*, 320 U.S. 591 (1944)	24

PAGE

Conclusion 29

Exhibit 1 – Chart of Terminated Units Pending Decision .....

Appendix (Separately Bound)

Decisions of the Supreme Court of Ohio Denying Rehearing (filed September 1, 1981) A-1, A-2, A-3

Mandates of the Supreme Court of Ohio (filed September 3, 1981) B-1, B-2, B-3

Decision and Opinion of the Supreme Court of Ohio (filed July 15, 1981) C-1

Decision and Opinion of the Public Utilities Commission of Ohio (filed July 10, 1980) D-1

Appellant's Notice of Appeal To The Supreme Court of the United States (filed September 2, 1981) E-1

Ohio Statutes: Ohio Revised Code §§ 4905.02, 4905.03, 4905.04, 4905.05, 4905.06, 4905.22, 4909.15, 4909.18, 4909.19, 4909.43; Ohio Administrative Code § 4901:1-9-05; Ohio Supreme Court Rule IX, Sections 1 and 2 ..... F-1

TABLE OF AUTHORITIES

CASES

	PAGE
Office of Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St. 2d 153, 423 NE 2d 820 (1981)	1
Re: Cleveland Electric Illuminating Co., Case No. 79-537-EL-AIR, *Opinion and Order*, Public Utilities Commission of Ohio 38 PUR 4th 494 (1980)	1, 3
Re: Virginia Electric & Power Company, 29 PUR 4th 65 (1979)	11
Bluefield Water Works v. Pub. Serv. Comm., 262 U.S. 679, 690 (1923)	15, 19, 20, 21, 29
Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944)	21, 24, 25, 26, 27, 29, 30
Southern Ca. Ed. Co., Opn. No. 821, Dkt. No. E-8176, 23 PUR 4th 44 (Fed. Pwr. Comm., 9/22/77)	22
La. Pwr. & Lgt. Co., Dkt. No. ER77-533 Phase I, (FERC, 2/12/79)	22
New England Pwr. Co., Opn. No. 49, Dkt. Nos. ER76-304, ER76-317, ER76-498, (FERC, 7/19/79)	22
Jersey Cen. Pwr. & Lgt. Co., Dkt. No. ER76-813, (FERC, 3/27/78)	22
Northern States Pwr. Co. (Minn.) – Northern States Pwr. Co. (Wis.), Dkt. No. ER79-616, (FERC, 12/4/80)	22
Alabama Pwr. Co., Dkt. No. 17667, (Ala. Pub. Ser. Comm.)	22
San Diego G. & Elec. Co., Case No. 90405, 31 PUR 4th 435 (Ca. Pub. Util. Comm., 6/5/79)	22
Southern Ca. Ed. Co., Case No. 81919, (Ca. Pub. Util. Comm., 8/1/72)	22

PAGE

Southern Ca. Ed. Co., Case No. 86794, (Ca. Pub. Util. Comm., 6/7/74) 22

Southern Ca. Ed. Co., Decision No. 87911, (Ca. Pub. Util. Comm. 12/ /78) 22

Potomac Elec. Co., Case No. 685, Order No. 6096, 29 PUR 4th 517, (D.C. Pub. Ser. Comm., 6/14/79) 22

Union Electric Co., Order No. 59835, (Ill. Comm. Comm., 12/10/75) 22

Ind. & Mich. Elec. Co., Case No. 35251 (Ind. Pub. Serv. Comm., 9/21/78) 22

Union Elec. Co., Dkt. No. U-558, (Iowa Comm. Comm., 11/14/75) 22

Potomac Elec. Pwr. Co., Order No. 6999, (Md. Pub. Serv. Comm., 1977) 22

Consumer Pwr. Co., Case No. F-700, (Mich. Pub. Serv. Comm., 2/10/75) 22

Detroit Ed. Co., Case No. F-762, (Mich. Pub. Serv. Comm., 7/26/76) 22

Detroit Ed. Co., Case No U-5108, (Mich. Pub. Serv. Comm., 5/27/77) 22

Union Elec. Co., Case No. ER77-154, (Mo. Pub. Serv. Comm., 1/19/78) 22

Pub. Serv. Elec. and Gas Co., Dkt. No. 794-310 OAL Dkt. No. PUC 877-79 (N.J. Dept. of Egy. – Bd. of Pub. Util., 4/11/80) 23

N.Y.S. Elec. & Gas Corp., Case Nos. 26432 and 26433, Order No. 74-12, (N.Y. Pub. Serv. Comm., 4/10/74) 23

PAGE

Rochester Gas and Elec. Corp., Orange and Rockland Util., Inc., Central Hudson Gas & Elec. Corp., and Niagara Mohawk Pwr. Corp., Opn. No. 81-1, Case No. 27794 (N.Y. Pub. Ser. Comm., 1/6/81) 23

Carolina Pwr. & Lgt. Co., Dkt. No. E-2, Sub. 366, (N.C. Util. Comm., 4/22/80) 23

Portland General Elec. Co., Case No. UF 3443, (Pub. Util. Comm. of Or., Order No. 79-055, 6/25/79) 23

Northern States Pwr. Co., Decision and Order No. F-3062, (S.D. Pub. Util. Comm., 10/6/76) 23

Gulf States Util. Co., Dkt. No. 2677, (Tex. Pub. Util. Comm., 10/29/79) 23

Houston Lgt. & Pwr. Co., Dkt. No. 2001, (Tex. Pub. Util. Comm., 12/5/78) 23

Houston Lgt. & Pwr. Co., Dkt. No. 2676, (Tex. Pub. Util. Comm.) 23

Va. Elec. & Pwr. Co., Case No. 19960, 29 PUR 4th 65 (Va. Corp. Comm., 3/19/79) 23

Appalachian Power Co., Case No. 9091, (W. Va. Pub. Serv. Comm., 5/3/78) 23

Wisc. Pub. Serv. Corp. v. Pub. Serv. Comm., Case No. 79CV809, (Wisc. Cir. Ct. II, 10/15/79, *aff'd*, Ct. of App. Dist. III, Case No. 79-1929, 10/7/80) 23

Re Arizona Public Service Co., Decision No. 51009 (Arizona Corp. Comm. 1980) 23

Re Northern States Pwr. Co., Case No. 10,097 (Pub. Serv. Comm. of N.D., 1980) 23

Federal Power Comm. v. Memphis Light, Gas & Water Div., 411 U.S. 458, at 465-466 (1973) 25

	PAGE
Permian Basin Area Rate Cases, 390 U.S. 747 (1978)	25
Webb's Fabulous Pharmacies, Inc. v. Bechwith, U.S. 49 U.S.L.W. 4033 (December 9, 1980)	25
Chicago, B & Q. R. Co. v. Chicago, 166 U.S. 226, 239 (1897)	25
Penn Central Transportation Co. v. New York City, 438 U.S. 104, 122 (1978)	25
Pacific Gas & Electric Co. v. City and County of San Francisco, 265 U.S. 403, 44 S.Ct. 537, 68 L.Ed. 1075 (1924)	26, 27
Missouri ex rel Southwestern Bell Tel. Co. v. Pub. Serv. Comm., 262 U.S. 276, at 290	27
Washington Gas Light Co., et al. v. Baker, 188 F.2d 11 (D.C. Cir. 1950), *cert. den.* 340 U.S. 952 (1951)	27, 28, 29

STATUTES

28 U.S.C. § 1257(2)	1
28 U.S.C. § 2103	2
Ohio Revised Code § 4905.13	14
Ohio Revised Code § 4905.18	15
Ohio Revised Code § 4905.22	2, 9, 11, 12, 13, 17, 20
Ohio Revised Code § 4909.15(A)(1)	14
Ohio Revised Code § 4909.15(A)(2)	15
Ohio Revised Code § 4909.15(A)(4)	2, 4, 10, 12, 16, 17, 19, 20, 21, 24, 25, 29, 30
Ohio Revised Code § 4909.18	3
Ohio Revised Code § 4909.43(B)	3
Ohio Administrative Code § 4901: 1-9-05	14

PAGE

CODE OF FEDERAL REGULATIONS (C.F.R.)

18 C.F.R. 101 14

AMENDMENTS

Fifth Amendment to the Constitution of the United States 2, 12, 20, 25

Fourteenth Amendment to the Constitution of the United States 2, 12, 20, 25

REPORTS OF OPINIONS BELOW

The Opinion of the Supreme Court of Ohio dated July 15, 1981 is reported at 67 Ohio St. 2d 153, 423 NE. 2d 820 (1981). The Court's denial of appellant's Motion For Rehearing is not officially reported. The Opinion and Order of the Public Utilities Commission of Ohio dated July 10, 1980 is reported at 38 PUR 4th 494 (1980). A copy of each of these decisions is included in the separate Appendix.

GROUNDS FOR JURISDICTION

This appeal is brought to review a 5-2 decision of the Supreme Court of Ohio reversing an Opinion and Order of the Public Utilities Commission of Ohio setting appellant's rates for electric utility service to retail customers in Ohio.

Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(2) to review the final judgment rendered on July 15, 1981 by the Supreme Court of Ohio, the highest court of the State of Ohio. Appellant's Motion for Rehearing was denied by the Ohio Court on September 1, 1981. Appellant filed its Notice of Appeal with the Supreme Court of Ohio on September 2, 1981.

The validity of Ohio Revised Code §§ 4909.15(A)(4) and 4905.22 was drawn into question before the Supreme Court of Ohio on the grounds that, as construed below for the first time, they are repugnant to the Fifth and Fourteenth Amendments to the Constitution of the United States, and the decision of the Supreme Court of Ohio was in favor of the validity of those statutes.

In the event that an appeal is not considered the proper mode of review, appellant requests that the papers upon which this appeal is taken be regarded and acted upon as a petition for writ of certiorari pursuant to 28 U.S.C. § 2103.

CONSTITUTIONAL PROVISIONS, STATUTES, AND REGULATIONS INVOLVED

1. The Fifth Amendment to the Constitution states, in pertinent part, as follows:

> "No person shall be . . . deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

2. The Fourteenth Amendment to the Constitution states, in pertinent part, as follows:

> "No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law . . . ."

3. Ohio Revised Code Section 4905.22, states, in pertinent part, as follows:

> "Every public utility shall furnish necessary and adequate service and facilities, and every public utility shall furnish and provide with respect to its business such instrumentalities and facilities as are adequate and in all respects just and reasonable."

4. Ohio Revised Code, Section 4909.15, states, in pertinent part, as follows:

> "(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, and charges shall determine:
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> • • •
>
> (4) The cost to the utility of rendering the public utility service for the test period . . . ."

STATEMENT OF THE CASE

A. The course of proceedings and their disposition in the courts below.

On June 19, 1979, Appellant, The Cleveland Electric Illuminating Company ("CEI") served and filed a Notice of its intent to submit a permanent rate increase application to The Public Utilities Commission of Ohio pursuant to Ohio Revised Code § 4909.18, as required by § 4909.43(B), and the Commission assigned to that Notice Case Number 79-537-EL-AIR. After the regular investigation by the Commission's Staff, the hearing began on April 12, 1980. The hearing lasted 32 trial days.

On July 10, 1980, The Public Utilities Commission of Ohio issued and entered in its Journal its Opinion and Order in Case No. 79-537-EL-AIR granting CEI an increase in rates. The Commission accepted the recommendation of its Staff and authorized as a part of allowable costs for rate-making purposes the amortization of the costs for planning, engineering, and initial construction associated with the construction of four nuclear generating units which had been cancelled and abandoned on January 23, 1980. The Commission allowed amortization of $56,437,000.00 in expenses over ten years.

Appellees, the Office of Consumers' Counsel (Case No. 80-1480), the Senior Citizens Coalition, et al. (Case No. 80-1528), and the City of Cleveland (Case No. 80-1547) appealed the decision of The Public Utilities Commission of Ohio to the Supreme Court of Ohio. Appellant, The Cleveland Electric Illuminating Company, participated in those cases as Intervening Appellee. On July 15, 1981, the Supreme Court of Ohio, in a 5-2 decision, reversed and remanded the July 10, 1980 Opinion and Order of The Public Utilities Commission of Ohio, holding that even where, as here, a capital expenditure for planning for future utility service was required by Ohio Revised

Code § 4905.22 for the convenience of the public and was prudent, the Commission nevertheless had no discretion to allow "the return *of* capital invested in failed projects" (67 Ohio St.2d at 167) under Ohio Revised Code § 4909.15(A)(4) as construed by the Ohio Court.

On July 24, 1981, CEI filed its Motion for Rehearing with the Supreme Court of Ohio. On September 1, 1981, the Supreme Court of Ohio denied the Company's Motion for Rehearing. Pursuant to Rule IX(2) of the Ohio Supreme Court Rules of Practice, that Court's mandate was issued at the same time rehearing was denied. On September 2, 1981, CEI filed with the Supreme Court of Ohio its Notice of Appeal to this Court and a Motion for Stay. The Ohio Court denied the Motion for Stay on September 11, 1981.

On September 16, 1981, the Public Utilities Commission of Ohio, by entry in Case No. 81-1096-EL-COI, initiated an investigation of appellant's present rates in light of the decision of the Supreme Court of Ohio at issue here. On September 22, 1981, CEI filed with this Court its Application for Stay of Execution and Enforcement of the Judgment of the Supreme Court of Ohio. (Case No. A-250). On September 29, 1981, CEI filed its Supplemental Brief. Briefs in opposition were filed by the Office of Consumers Counsel, the City of Cleveland, and the Senior Citizens Coalition. On October 8, 1981, CEI filed its Reply Brief. This Court denied the requested Stay on October 12, 1981.

On October 21, 1981, the Commission ordered appellant to submit tariffs reducing its present rates by an amount equal to the revenue requirements attributable to the cancelled nuclear facilities. On October 28, 1981, the Public Utilities Commission of Ohio approved the tariffs submitted and thus reduced appellant's rates, effective October 28, 1981, pending a decision in this case by this Court.

B. The facts material to the questions presented.

In 1967, The Cleveland Electric Illuminating Company joined with four other electric utilities (Ohio Edison, Toledo Edison, Duquesne Light and Pennsylvania Power) in an organization, the Central Area Power Coordination Group (CAPCO), for the joint planning, construction and operation of electric generating facilities. The objective was to obtain economies of scale and the increased service reliability which would arise from participation in such an organization.

CAPCO was formed to jointly plan, construct and operate "base load" generation capacity, i.e. very large generating units which are intended to be less expensive to operate at a relatively constant level of production. Since such base load units require extremely long construction lead times and, therefore, must be planned and committed many years in advance, the CAPCO companies established detailed planning procedures based on long-range forecasts. If, after later forecasts are made, lower future loads are predicted than had been forecasted years previously, construction of a base load unit or units may be postponed or even cancelled. In contrast, however, if future load proves to be higher than previously forecasted, base load capacity can not be constructed quickly enough to meet that load. This requires the construction of "peaking" capacity, i.e. much smaller oil-fired generators with a shorter construction lead time, but much higher overall costs to consumers, even where oil is available and its use compatible with national energy goals, to meet the additional load. The CAPCO companies regularly reviewed their respective load forecasts and devised the construction program based on them intended to provide reliable and economical generation capacity as needed.

In early 1973, the CAPCO companies, acting on the best forecasts and information available to them at that time, entered into commitments to construct the four nu-

clear units giving rise to this case – Davis Besse Units ※2 and ※3 and Erie Units ※1 and ※2 – in order to supply the required adequate amount of electric power to the public in 1983 and thereafter. Pursuant to that decision, appellant (along with its CAPCO partners) began investing capital to plan, engineer and start initial construction of the four units. Subsequent developments, not the least of which was the Arab Oil Embargo (which no one could have anticipated), resulted in a reduction of the forecasted rate of growth in the demand for power in the CAPCO area. The CAPCO companies, including CEI, repeatedly reviewed and updated their forecasts in the light of these new developments.

On several occasions CAPCO postponed the four planned units, so that their expected in-service dates would fit the newly forecasted loads,[1] i.e. they would be available when needed, but not before then. The companies continued to study a variety of alternatives in light of the most recent forecasts, such as the substitution of coal-fired base load units. However, in each instance, it was the judgment of all of the CAPCO companies, as well as the individual judgment of The Cleveland Electric Illuminating Company, that the construction program, as postponed from time to time to fit the revised forecasts, was the most practical and economic program in the circumstances known when each decision was made.

Yet another unanticipated factor was added in early 1979, when the Three-Mile Island incident resulted in sharply increased political and regulatory uncertainty regarding the construction and operation of nuclear generating plants. The Three-Mile Island unit was constructed by Babcock and Wilcox, the same company which had

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[1]For example, the entire program was slipped back one year in 1974, reducing CEI's five year construction program from $1,234,000,000 to $1,194,000,000. The construction of the four units was slipped back again in 1975, 1976, 1977 and late 1978.

already constructed a licensed and operating nuclear generation unit known as Davis-Besse Unit №1 for some of the CAPCO companies, including CEI. Before TMI it had been anticipated that Davis-Besse Unit №1 would be replicated in the construction of the four planned units, so that new ground (with respect, for example, to design) would not have to be broken, with attendant savings.

However, after TMI, it began to become apparent that the substantial savings anticipated by CAPCO from replicating the existing Davis-Besse Unit №1 when Davis-Besse №2 and №3 and Erie №1 and №2 were constructed would not occur. Davis-Besse №2 and №3 and Erie №1 and №2 were exposed to drastic design change requirements and to unpredictable future licensing, design, construction, and operation requirements by the Nuclear Regulatory Commission, and this became a significant consideration to the CAPCO companies. It became certain that a complete duplication of Davis-Besse Unit №1 as originally constructed would be impossible. Further, continual re-engineering, re-manufacture of fabricated parts, and retrofitting of new requirements were expected to cause a further substantial increase in the cost of the four planned units.

These considerations resulted in a decision to terminate the planning for the four units on January 22, 1980. CEI had dedicated $56,437,000.00 toward planning, engineering and initial construction costs on those units.[2]

At the time of the decision to cancel the four nuclear units, CEI had pending before the Public Utilities Commission of Ohio an application for a general increase in

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[2]The other utilities belonging to CAPCO had also dedicated substantial amounts to planning the four cancelled plants. Ohio Edison had dedicated approximately $85.5 million. Toledo Edison had dedicated approximately $24.5 million. Duquesne Light had dedicated approximately $35 million. Pennsylvania Power had dedicated approximately $16 million.

rates. The Company requested an expense adjustment to amortize over a ten-year period the after-tax amount which had been dedicated to planning and engineering the construction projects for the four generating units. CEI did not request that the unamortized balance of these expenses be included in rate base so that it could earn a return *on* the investment, a form of relief which had been allowed in similar circumstances by a number of jurisdictions. In effect, CEI proposed simply to restore the investor's investment to the investor over a ten-year period (similar to the recovery *of* investment which would have been achieved through depreciation if the plants had gone into service), but *not* to provide the investor with any return *on* the unrestored portion of that investment over the ten-year amortization period.

Thereafter, the Staff Report of Investigation was filed and public hearings commenced on April 2, 1980, running for thirty-two (32) hearing days. Mr. Harold Williams, Executive Vice President of The Cleveland Electric Illuminating Company, testified at length regarding the decision-making processes of The Illuminating Company and CAPCO. Mr. William Masters, Manager of System Planning Engineering for CEI, testified at length regarding the long-range forecasting done by The Illuminating Company. Mr. Edgar Maugans, Vice-President, Finance, for CEI, and Mr. Francis Jeffries, Executive Vice President of Duff and Phelps, Inc., an investment research organization, testified as to the rate of return required by the Company. Both Mr. Maugans and Mr. Jeffries explicitly testified that the investor had not been compensated through rate of return for the risk that the planning expenses would be excluded entirely from cost of service.

Mr. Said Hanna, Chief of the Commission's Accounting Section, and Mr. Randy Farrar, Senior Financial Analyst of the Commission's Finance and Economics Division, both recommended approval of the proposed amortization as part of appellant's cost of service.

On July 10, 1980, The Public Utilities Commission issued its Opinion and Order finding that the planning costs were prudently incurred at every step of the decision-making process and adopting the recommendation of its staff that CEI be authorized to recover the costs by amortizing over a ten-year period the expenses associated with the planning of the four units. This decision was consistent with the decisions of every Federal and State regulatory agency theretofor presented with such a question in similar circumstances.

C. The decision of the Supreme Court of Ohio.

On July 15, 1981 the Supreme Court of Ohio affirmed the Commission in all its findings of fact and on all legal issues, except one. Regarding the includability of appellant's reasonable and prudent costs for planning, engineering, and initial construction of the four cancelled generation plants as allowable costs for ratemaking purposes, the Court reversed and remanded.

In doing so, the Court rejected what the Court itself described as "the overwhelming weight of authority from other jurisdictions." (67 Ohio St.2d at 162). The Ohio Court also rejected the specifications of the Uniform System of Accounts prescribed for electric utilities by the Federal Energy Regulatory Commission in the Code of Federal Regulations and by the Public Utilities Commission of Ohio in the Ohio Administrative Code.

The Ohio Court agreed that Ohio Revised Code § 4905.22 required CEI to invest this capital because it "require[s] utilities to maintain adequate service presently and for the foreseeable future." (67 Ohio St.2d at 163). The Ohio Court agreed with the Commission's finding that the expenditures were prudently dedicated for the convenience of the public pursuant to the requirement of § 4905.22 that a public utility provide adequate service and facilities.

The Ohio Court held that "notwithstanding the provisions that impose a duty on utility companies to plan for the future . . ." (67 Ohio St.2d at 163), the Commission did not have the power to include these planning expenses in cost of service because they were not "normal, recurring expenses" within the meaning of the Court's definition, for the first time, of the word "cost" in Ohio Revised Code § 4909.15(A)(4).

Appellant filed a Motion for Rehearing with the Supreme Court of Ohio arguing that to construe the word "cost" in this way, for the first time in this case, was to construe the statute to require the Commission to confiscate the property of CEI in violation of the Fifth and Fourteenth Amendments to the Constitution. The Supreme Court of Ohio denied appellant's Motion for Rehearing, thereby deciding in favor of the validity of those statutes, as so construed.

D. The stage at which the question sought to be reviewed was raised below.

CEI alerted the Ohio Supreme Court in its first brief in this case of the constitutional problem which might arise if the Ohio ratemaking formula were construed to prohibit recovery of necessary and prudent planning costs in some fashion. In its Brief Of Intervening Appellee to the Ohio Court in support of the Ohio Commission's decision allowing the planning costs in cost of service, CEI emphasized the expertise of the Commission in these matters, the unanimity of expert testimony in the hearing supporting the accounting procedures followed, the requirements of the FERC Uniform System of Accounts, and the overwhelming weight of authority from other jurisdictions supporting the Ohio Commission's decision.

In emphasizing the reasonableness of the request which had been allowed by the Commission, CEI pointed out to the Ohio Court that many other Commissions had

granted *rate base treatment* of the unamortized portion of such expenses (thereby allowing both the return *of* the capital and a return *on* the investment), and that at least one school of thought held that such rate base treatment, which would have constituted greater relief than that sought before and allowed by the Ohio Commission, was constitutionally required.

In support of its argument that even more relief than that granted by the Ohio Commission might be constitutionally required, CEI cited and quoted an opinion of Virginia Commissioner Shannon in *Re: Virginia Electric & Power Company,* 29 PUR 4th 65 (1979) in which he dissented from a decision which gave VEPCO *only* the relief sought here by CEI and granted by the Ohio Commission:

> "Perhaps a more succinct way to state the proposition would be as follows: The investor is *constitutionally* entitled to *just compensation* for prudent expenditures. The rate-making mechanism must provide for a return *on* the investment and the return *of* the investment. Because depreciation rates are not calculated to include the probabilities of extraordinary property losses, it is necessary to amortize the loss of Surry Units 3 and 4. Further, because rates of return have not compensated the investor for the risk of this extraordinary property loss, the unamortized balance should be included in the Company's rate base until the loss is completely amortized."
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> (29 PUR 4th at 96, emphasis added).

Therefore, CEI was subsequently surprised by the Ohio Court's novel and unprecedented opinion construing the word "cost" in Ohio Revised Code § 4909.15(A)(4) to prohibit the Public Utilities Commission of Ohio from allowing even the recovery *of* (much less earnings *on*) necessary and prudent planning costs required by Ohio Revised Code § 4905.22. CEI explicitly attacked the

validity under the Fifth and Fourteenth Amendments of those particular statutes, as construed, at its earliest opportunity after the unconstitutional construction was rendered, in its Motion for Rehearing[3] to the Ohio Supreme Court filed on July 24, 1981. The Ohio Court decided in favor of the constitutionality of Ohio Revised Code § 4905.22 and § 4909.15(A)(4) when it decided against appellant's Motion for Rehearing on September 1, 1981.

REASONS REQUIRING PLENARY CONSIDERATION

I. OHIO REVISED CODE § 4905.22 and § 4909.15 (A)(4), AS CONSTRUED BY THE SUPREME COURT OF OHIO, DIRECTLY CONFLICT WITH THE PROSCRIPTION OF THE FIFTH AND FOURTEENTH AMENDMENTS TO THE CONSTITUTION OF THE UNITED STATES PROHIBITING CONFISCATION OF PRIVATE PROPERTY WITHOUT DUE PROCESS OF LAW.

The principal reason for appeal of this case to this Court is to test whether Ohio Revised Code § 4905.22 and § 4909.15(A)(4) may constitutionally require a public utility to invest its capital in the present to provide adequate service to the public in the future, but may deny recovery *of* that invested capital even where it is found that the capital was prudently and reasonably invested for the convenience of the public for planning, engineering, and initial construction of electric generating units pursuant to the statutory requirement.

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[3] A copy of CEI's Motion for Rehearing has previously been supplied to this Court as Exhibit 3 to CEI's Application For Stay. (Case No. A-250).

Ohio Revised Code § 4905.22, states, in pertinent part, as follows:

> "Every public utility *shall furnish* necessary and *adequate* service and *facilities*, and every public utility shall furnish and provide with respect to its business such instrumentalities and facilities as are adequate and in all respects just and reasonable."

There is no question that this statute requires appellant, as a public utility, to invest its capital in the present for planning and engineering for the convenience of the public to furnish adequate facilities in the future. The plain words of the statute say so, and the Ohio Court so held. (67 Ohio St. 2d at 163). An electric utility serving 700,000 customers plainly cannot operate without planning and engineering for the future. Large base-load generating units, which have the advantage of being energy efficient, simply cannot be built without a lead-time exceeding ten (10) years. The record overwhelmingly supports the Commission's factual finding that the expenses at issue were proper business expenses which were prudently incurred. The Ohio Court did not disturb that finding.

Likewise, there is no question in this case that the capital invested by appellant for planning and engineering these generating units was dedicated to the convenience of the public as required by this statute. No party argued otherwise. The Ohio Commission noted that "What the company seeks is the recovery of costs incurred on behalf of its ratepayers to assure that adequate service could be maintained." (Quoted by the Ohio Court at 67 Ohio St. 2d at 161). The Supreme Court of Ohio also found that the appellant's investment was dedicated to the convenience of the public:

> "The now terminated nuclear plants represented a major capital investment that ultimately *would have*

> *been included in the rate base* under R. C. 4909.15 (A)(1), had the projects not been cancelled."
>
> (67 Ohio St. 2d at 164).

Ohio Revised Code § 4909.15(A)(1), cited by the Ohio Court, limits a utility's rate base to that which is "used and useful in rendering the public utility service . . ." In other words, by acknowledging that the investment would have been included in rate base, the Ohio Court agreed that the investment was dedicated to the convenience of the public.

The accounting treatment for the capital invested in such required construction is, for a public utility, tightly circumscribed. Decades ago the Federal Energy Regulatory Commission (then the Federal Power Commission) adopted a Uniform System of Accounts, and required utilities subject to its jurisdiction, including CEI, to use it. *See* 18 C.F.R. 101. The Public Utilities Commission of Ohio, pursuant to its authority under Ohio Revised Code § 4905.13, also adopted it, effective January 1, 1961, and required Ohio utilities to use it. *See* Ohio Administrative Code § 4901: 1-9-05. For the entire period from 1973 to 1979 during which CEI was prudently and reasonably spending this money to plan, engineer, and begin construction of these four now-cancelled plants, CEI was required by law to account for this money in certain ways, which it did.

Under the Uniform System of Accounts, planning and engineering expenditures of this kind are not ordinarily shown on a utility's books as operating expenses when made, but are capitalized. Thus, they increase the eventual book cost of the property to which they relate. Since the property is under construction, these expenditures must be booked in Account No. 107 (construction work in progress). Eventually, when the property is completed and goes into service, the investment would ordinarily be transferred on the books to Account No. 101 (plant in service).

In such case, the dedicated capital investment (including the kinds of planning and engineering expenses here under discussion) would then be recovered, over the property's life, through depreciation accruals, for which explicit provision is made in the Ohio statutes. Ohio Revised Code § 4905.18 guarantees to the investor in utility property the recovery *of* at least the original cost of the investment by depreciation accruals. The investor would also earn a return *on* this capital investment after it went into service, since it would become part of the utility's rate base and earn a rate of return.

So far, as the Court can see, we have been talking of expenditures which become part of a utility's rate base. In such case, the investor will, consequently, be entitled not only to recovery *of* the original cost of that property, through depreciation accruals, but also to earn a fair and reasonable rate of return *on* that rate base property. *See* Ohio Revised Code § 4909.15(A)(2); *see also Bluefield Water Works v. Pub. Serv. Comm.*, 262 U.S. 679, 690 (1923). Stated another way, the investor is not only entitled to get his original money back, but also to have an opportunity to earn a profit on his investment.

When CEI prudently and reasonably determined that the four planned generating units should be cancelled, the FERC Uniform System of Accounts adopted in the Ohio Administrative Code required that the accounting be performed in a very specific way. The invested dollars, previously recorded in a "plant" account (Account 107, Construction Work In Progress) were moved to an "expense" account (Account 182, Extraordinary Property Losses) when the units were cancelled.

The *unanimous* testimony of the expert accounting witnesses, including Mr. Hanna, the Chief Accounting Officer for the Public Utilities Commission, was that this procedure was proper.

Since it is undisputable on this record that we are dealing here with a *cost,* or *expense,* the question becomes how that cost, or expense, is to be treated for rate-making purposes.

The Commission held that these costs should be recognized for rate-making purposes as a "cost" of service under Ohio Revised Code § 4909.15(A)(4), and allowed amortization of these costs over ten years. The undisputed evidence showed that the vast majority of future ratepayers are present ratepayers, so the planning costs were not only a present benefit to present ratepayers (since the community must be able to rely today on the assurance of adequate service tomorrow) but were also a present benefit to most of the ratepayers of the future. The Supreme Court of Ohio did not disturb a single finding of fact but nevertheless reversed.

Ohio Revised Code, Section 4904.15, states, in pertinent part, as follows:

> "(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, and charges shall determine:
>
> • • •
>
> (4) The *cost* to the utility of rendering the public utility service for the test period. . . ."

The Supreme Court of Ohio, in the decision below, held for the first time, without citation to authority, and contrary to the provisions of the Uniform System of Accounts, that the word "cost" in this statute prohibits the Public Utilities Commission from including in cost of service any cost other than "normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period." (67 Ohio St.2d at 164). The Ohio Court ignored the construction of the word "cost" which had been present in the Ohio Administrative Code for decades. The Ohio Court cited no legislative history. The Ohio

Court held that the Commission may not include in cost of service any capital expenditures by a public utility, whether or not they were prudent and whether or not they were expended for the public convenience, if the expenditures were not "normal, recurring expenses." Thus, Ohio Revised Code § 4905.22 requires a public utility to dedicate its capital to the planning and engineering of future generating plants, and Ohio Revised Code § 4909.15(A)(4), as now construed, prohibits the Commission from providing for recovery *of* those same expenditures through rates. Appellant submits that is a confiscation of its property without due process of law.

This case does not present any conflict in the evidence. No evidence whatsoever was offered before the Commission that it was not reasonable or prudent to commit these four units, to dedicate capital to plan and engineer them, or to cancel them.

The Commission found that the company's decisions "were reasonable and prudent at every step of this process" and the Supreme Court of Ohio did not disturb that finding. (*See* 67 Ohio St. 2d at 162-163).

No evidence whatsoever was offered before the Commission below that the Company or investors in its securities were compensated in any way, through the rate of return authorized in this or previous rate proceedings or otherwise, for the risk that these prudent expenses dedicated to the public convenience would be entirely excluded from cost of service. On the contrary, every witness who addressed the issue, including the Commission's Chief Accounting Officer, testified that the stockholders had *not* been compensated for the risk that these prudent expenses would be excluded from cost of service. There should be no mistake about the testimony of the expert witnesses on this point. Mr. Maugans, Vice-President, Finance, for CEI, testified that:

> "Until now, this Commission has not been presented with the possibility that investors may ultimately be

> confronted with the risks of noncompletion of prudently invested capital projects. *This kind of risk has not been reflected in the rates of return levels granted by the Commission.* Utility shareowners are entitled to just compensation for capital invested in enterprises providing public service. If the shareowners must assume additional risks, *they will demand a greater return on their investment.*"

Mr. Francis Jeffries, Executive Vice President of Duff and Phelps, Inc., an investment research organization, testifying as an expert on rate of return on behalf of CEI, said that investors were aware that this issue had been consistently decided in favor of some sort of amortization in other jurisdictions and had established a market price for utility stocks which assumed only the risk of exclusion of imprudent investments by the utility. Commission Staff witnesses Said Hanna and Randy Farrar agreed.

The confiscation of The Illuminating Company's property is clear if the numbers used by the Commission in its July 10, 1980 Opinion and Order are revised to reflect the removal of the amortization of the cancellation costs allowed by the Commission and to reflect the required one-time write-off of the entire $56.4 million. The Commission found the Company's existing rate of return of 8.39% to be unreasonable, (*Opinion and Order,* page 46) and found a rate of return of 10.82% to be fair and reasonable. The Ohio Court has not disturbed that finding. If the amortization is removed, and if the entire $56.4 million is assumed to have been written off (as the Commission found was required by the Uniform System of Accounts and as the Ohio Court has now ordered), The Illuminating Company's tariffs in this case, all other things being equal, would produce only an 8.6% return, even assuming that the allowed revenues were actually achieved, a highly unlikely assumption.

The same calculation, done on the actual results for The Illuminating Company for 1980 as reported in its An-

nual Report, would yield a rate of return of only 6.4%. This figure may be fairly contrasted to the Commission's *Opinion and Order* of May 4, 1981, in The Illuminating Company's most recent rate case (Case No. 80-376-EL-AIR), wherein the Commission found the achieved rate of return of 7.45%, *including* the amortization of the costs at issue here, to be unjust and unreasonable and authorized an overall rate of return of 11.76%. (*Opinion and Order,* pp. 53-54). It is the rates set in this later case which have now been reduced by the Commission in response to the Ohio Court's decision. Clearly the effect of Ohio Revised Code § 4909.15(A)(4), as applied, unconstitutionally confiscates the Company's property, not only by denying the Company recovery of the money, but also by reducing the Company's overall rate of return below the level *found* by the Commission to be *unjust* and *unreasonable.*

In *Bluefield Water Works Co. v. Public Service Commission of West Virginia,* 262 U.S. 679 (1923), the United States Supreme Court declared the requirements of the United States Constitution regarding state regulation of utility rates:

> "A public utility is entitled to such rates as will permit it to earn a return *on* the value of the property which it employs for the convenience of the public equal to that generally being made at the same time, and in the same general part of the country on investments in other business undertakings which are attended by *corresponding risks* and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economical management, to maintain its credit, and enable it to raise the money *necessary for the proper discharge of its public duties.*" (262 U.S. at 692-93, emphasis added).

The Court further stated that rates which fail to satisfy this standard

> "are confiscatory and therefore beyond legislative power. Rates which are not sufficient to yield a reasonable return *on* the value of the property used at the time it is being used to render the service are *unjust, unreasonable* and *confiscatory,* and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment." (262 U.S. at 690, emphasis added).

As construed and applied below, Ohio Revised Code § 4905.22 and § 4909.15(A)(4) are unconstitutional by reason of repugnancy to the Fifth and Fourteenth Amendments to the United States Constitution. The Ohio Court's Opinion in this case construes Ohio Revised Code § 4909.15(A)(4) so as to confiscate the prudent expenditures of CEI, and its stockholders, dedicated to fulfillment of its current statutory obligation to serve in the future. Simply put, Ohio Revised Code § 4905.22 requires CEI to spend money and Ohio Revised Code § 4909.15(A)(4), as now applied by the Ohio Court, prevents CEI from receiving even a return *of* that money, much less *on* that money. That is an unconstitutional confiscation of property in violation of the Fifth and Fourteenth Amendments of the Constitution.

Phrased in the words of the *Bluefield* case, the Ohio Court has construed Ohio Revised Code § 4909.15(A)(4) so that it denies to CEI the opportunity "to earn a return on the value of the property it employs for the convenience of the public. . . ." There can be no debate that this "property" was "employed for the convenience of the public. . . ." The Commission found that the expenditures were reasonably and prudently made "at every step of this process." The Ohio Court has not disturbed that finding. Yet, the statute, as construed by the Ohio Court, has denied CEI the opportunity even to recover the "property."[4]

[4]Note that CEI did not propose, and the Commission did not allow, CEI to earn *on* this investment. There is no return or, in layman's terms, "profit", involved at all in this case.

Moreover the inevitable effect of construing Ohio Revised Code § 4909.15(A)(4) so as to preclude CEI from recovering such prudent planning expenditures as part of its cost of service is to reduce CEI's effective overall net rate of return on its property employed for the convenience of the public below a level which is fair, just, and reasonable under the *Bluefield* standard. As construed by the Ohio Court in this case, Ohio Revised Code § 4909.15(A)(4) requires the Commission to exclude prudent planning expenditures incurred by a utility even though such expenditures would clearly be regarded as legitimate costs of business if incurred by a non-regulated business concern and would be recovered in the price of its product or service. As a consequence, what might otherwise be a fair and reasonable net return, where such planning costs are included, becomes unconstitutionally unfair and unreasonable if the utility incurs such prudent expenditures, which, as in this case, may be quite large in magnitude, but is not permitted to include such costs in determining the net return on its property.

Just as the West Virginia Commission in *Bluefield* was not permitted, consistently with the U.S. Constitution, to utilize an artificially low valuation of the utility's rate base property in arriving at the amount of a fair and reasonable return, so the State of Ohio in this case cannot, by statutory mandate or otherwise, be permitted to utilize an artificially low determination of CEI's cost of service in calculating the net return allowable to CEI, if such return, net of the actual costs incurred by CEI, would not be fair and reasonable under *Bluefield* and like decisions of the Supreme Court of the United States.

This issue is of great importance to utilities of all kinds throughout the United States. Ohio Revised Code § 4909.15, which was construed below, uses the "just and reasonable" standard used by this Court in *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) and in virtually every ratemaking statute in every state. The Office of Consumers' Counsel, appellants below, has

publicly claimed that the Ohio Court's decision is a national precedent.

The decision of the Supreme Court of Ohio is unprecedented and directly conflicts with decisions in many other state jurisdictions as well as decisions of the Federal Energy Regulatory Commission, the federal regulatory agency having jurisdiction over such matters. Until the decision below, no court or commission had denied a utility the opportunity to recover reasonable and prudent planning and engineering costs incurred for the convenience of the public in their respective jurisdictions where the planned unit was subsequently cancelled in similar circumstances. The Federal Energy Regulatory Commission and at least eighteen (18) other utilities commissions have allowed the recovery of such costs for terminated facilities.[5] (Two utilities commissions have refused to allow such costs to be *allocated* to ratepayers in *their* jurisdictions where the cancelled facilities were planned for, and the cancellations were caused

[5] *Southern Ca. Ed. Co.*, Opn. No. 821, Dkt. No. E-8176, 23 PUR 4th 44 (Fed. Pwr. Comm., 9/22/77); *La Pwr. & Lgt. Co.*, Dkt. No. ER77-533 Phase I, (FERC, 2/12/79); *New Eng. Pwr. Co.*, Opn. No. 49, Dkt. Nos. ER76-304, ER76-317, ER76-498, (FERC, 7/19/79); *Jersey Cen. Pwr. & Lgt. Co.*, Dkt. No. ER76-813, (FERC, 3/27/78); *Northern States Pwr. Co. (Minn.) – Northern States Pwr. Co. (Wis.)*, Dkt. No. ER79-616, (FERC, 12/4/80); *Alabama Pwr. Co.*, Dkt. No. 17667, (Ala. Pub. Ser. Comm.); *San Diego G. & Elec. Co.*, Case No. 90405, 31 PUR 4th 435 (Ca. Pub. Util. Comm., 6/5/79); *Southern Ca. Ed. Co.*, Case No. 81919, (Ca. Pub. Util. Comm., 8/1/72); *Southern Ca. Ed. Co.*, Case No. 86794, (Ca. Pub. Util. Comm., 6/7/74); *Southern Ca. Ed. Co.*, Decision No. 87911, (Ca. Pub. Util. Comm. 12/ /78); *Potomac Elec. Co.*, Case No. 685, Order No. 6096, 29 PUR 4th 517, (D.C. Pub. Ser. Comm., 6/14/79); *Union Elec. Co.*, Order No. 59835, (Ill. Comm. Comm., 12/10/75); *Ind. & Mich. Elec. Co.*, Case No. 35251 (Ind. Pub. Serv. Comm., 9/21/78); *Union Elec. Co.*, Dkt. No. U-558, (Iowa Comm. Comm., 11/14/75); *Potomac Elec. Pwr. Co.*, Order No. 6999, (Md. Pub. Serv. Comm., 1977); *Consumer Pwr. Co.*, Case No. F-700, (Mich. Pub. Serv. Comm., 2/10/75); *Detroit Ed. Co.*, Case No. F-762, (Mich. Pub. Serv. Comm., 7/26/76); *Detroit Ed. Co.*, Case No. U-5108, (Mich. Pub. Serv. Comm., 5/27/77); *Union Elec. Co.*, Case No. ER77-154, (Mo.

by, other jurisdictions).[6] The decision below is the only state supreme court decision on the issue.

This case is of extreme national importance for the additional reason that similar cases are now pending or imminent before state commissions all over the country. At the present moment, there are pending in the United States at least seventeen (17) other applications to utilities commissions to include in rates planning and engineering costs for twenty-four (24) electric generation facilities which have been terminated and in which the utilities have invested *at least* $598.9 million.[7] The constitutional issues raised by this case will affect all of those pending applications.

Pub. Ser. Comm., 1/19/78); *Pub. Serv. Elec. and Gas Co.*, Dkt. No. 794-310 OAL Dkt. No. PUC 877-79, (N.J. Dept. of Egy.—Bd. of Pub. Util., 4/11/80); *N.Y.S. Elec. & Gas Corp.*, Case Nos. 26432 and 26433, Order No. 74-12, (N.Y. Pub. Serv. Comm., 4/10/74); *Rochester Gas and Elec. Corp., Orange and Rockland Util., Inc., Central Hudson Gas & Elec. Corp., and Niagara Mohawk Pwr. Corp.*, Opn. No. 81-1, Case No. 27794 (N.Y. Pub. Ser. Comm., 1/6/81); *Carolina Pwr. & Lgt. Co.*, Dkt. No. E-2, Sub. 366, (N.C. Util. Comm., 4/22/80); *Portland General Elec. Co.*, Case No. UF 3443, (Pub. Util. Comm. of Or., Order No. 79-055, 6/25/79); *Northern States Pwr. Co.*, Decision and Order No. F-3062, (S.D. Pub. Util. Comm., 10/6/76); *Gulf States Util. Co.*, Dkt. No. 2677, (Tex. Pub. Util. Comm., 10/29/79); *Houston Lgt. & Pwr. Co.*, Dkt. No. 2001, (Tex. Pub. Util. Comm., 12/5/78); *Houston Lgt. & Pwr. Co.*, Dkt. No. 2676, (Tex. Pub. Util. Comm.); *Va. Elec. & Pwr. Co.*, Case No. 19960, 29 PUR 4th 65 (Va. Corp. Comm. 3/19/79); *Appalachian Power Co.*, Case No. 9091, (W.Va. Pub. Serv. Comm., 5/3/78); *Wisc. Pub. Serv. Corp. v. Pub. Serv. Comm.*, Case No. 79CV809, (Wisc. Cir. Ct. II, 10/15/79, *aff'd*, Ct. of App. Dist. III, Case No. 79-1929, 10/7/80).

[6] *Re Arizona Public Service Co.*, Decision No. 51009 (Arizona Corp. Comm. 1980); *Re Northern States Pwr. Co.*, Case No. 10,097 (Pub. Serv. Comm. of N.D., 1980).

[7] Attached to this Jurisdictional Statement as Exhibit 1 is a chart showing the most recent information appellant could obtain regarding these 24 cancelled generating units. The Bailey Unit was cancelled by NIPSCO on August 26, 1981.

II. OHIO REVISED CODE § 4905.22 AND 4909.15. (A)(4), AS CONSTRUED BELOW, DIRECTLY CONFLICT WITH THIS COURT'S DECISION IN *FEDERAL POWER COMMISSION V. HOPE NATURAL GAS CO.*, 320 U.S. 591 (1944)

A second major reason for appeal in this case is to test the ruling by the Supreme Court of Ohio that Ohio Revised Code § 4909.15(A)(4) as construed below, may constitutionally exclude prudent planning expenses incurred for the convenience of the public from a utility's allowable expenses for ratemaking purposes, where the risk of such exclusion has not been considered in setting the fair rate of return, thereby reducing the utility's effective overall net rate of return below the level expressly found to be fair, just, and reasonable.

In *Hope, supra,* this Court upheld the use of an original cost/prudent investment "rate base" as constitutional, emphasizing that the overall objective in ratemaking is not the method employed, but the maintenance of the integrity of the utility's investment. The Court emphasized that basing depreciation expense on original cost assured that ". . . the utility is made whole and the integrity of its investment is maintained. No more is required." (302 U.S. at 606). Thus, the test applied by the Court in evaluating whether the 'result reached' was constitutional was twofold: 1) whether the utility was "made whole," in terms of original cost, and 2) whether the "integrity of its investment" was maintained.

The Court also noted that the "financial integrity of the company" required "enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock." (320 U.S. at 603). The Court summarized the elements required to meet the just and reasonable test of the Natural Gas Act and to avoid confiscation:

> "Rates which enable the company to operate successfully, to maintain its financial integrity, to attract capital, and *to compensate its investors for the risks as-*

> *sumed* certainly cannot be condemned as invalid, even though they might produce only a meager return on the so-called "fair value" rate base." (320 U.S. at 605).

The criteria of *Hope* were reiterated recently in *Federal Power Comm. v. Memphis Light, Gas & Water Div.*, 411 U.S. 458, at 465-466 (1973).

In *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), the Court said that:

> ". . . the just and reasonable standard of the Natural Gas Act 'coincides' with the applicable constitutional standards, *FPC v. Natural Gas Pipeline Co., supra*, at 586, and any rate selected by the Commission from the broad zone of reasonableness permited by the Act cannot properly be attacked as confiscatory." (390 U.S. at 770).

Thus, the criteria announced in *Hope* are the criteria for measuring confiscation in violation of the Fifth Amendment.

The confiscation clause of the Fifth Amendment is applicable to the states through the due process clause of the Fourteenth Amendment. *Webb's Fabulous Pharmacies, Inc. v. Bechwith*, 449 U.S. 155, 160 (December 9, 1980), citing *Chicago, B & Q. R. Co. v. Chicago*, 166 U.S. 226, 239 (1897) and *Penn Central Transportation Co. v. New York City*, 438 U.S. 104, 122 (1978).

Applying these criteria to this case shows clearly that Ohio Revised Code § 4909.15(A)(4), as construed below, confiscates appellant's property. It is undisputed that appellant's capital was expended for the convenience of the public pursuant to appellant's statutory obligation to plan and engineer its utility system to serve adequately in the future. It is undisputed that the initiation of the project, the planning costs themselves, and the termination of the project, were all prudent. Finally, it is undisputed that the appellant's investors have not been compensated through rate of return, either in this case or in prior ones, for the unanticipated risk that these planning expenses would be excluded from cost of service for ratemaking purposes. Specifically, in this case the fair rate of return allowed assumed

the inclusion of these expenses for ratemaking purposes. The Public Utilities Commission of Ohio included these expenses in the allowable cost of service and established both the rate of return and the amount of the total rate increase on that basis. As construed below, Ohio Revised Code § 4909.15(A)(4) prohibits the Commission from setting rates which "compensate [appellant's] investors for the risks assumed . . ." *Hope, supra*, at 605.

In *Pacific Gas & Electric Co. v. City and County of San Francisco*, 265 U.S. 403, 44 S.Ct. 537, 68 L.Ed. 1075 (1924), a case which preceded the Court's *Hope* decision but which is nevertheless important here, the Court held that it was error for the District Court to employ in cost of service the reduced costs of manufacturing gas made possible by new inventions but to exclude from the valuation of the rate base both the proper valuation for the patented inventions and the value of the old abandoned utility property. Obviously, we do not face precisely the same rate base issue here.

The importance of *Pacific Gas* here is that this Court placed particular emphasis on the facts that 1) the patents which rendered the old gas plant obsolete "were of recent conception," 2) that the utility could not have provided for the obsolescence of the old plant through depreciation charges in previous rates, and 3) that the obsolescence "could not have been long anticipated."

The analogy to the present case is apparent. The reasons for the accounting change which moved CEI's expenses from a rate base account to an expense account, the reasons for the termination of the units, were of "recent conception" and "could not have been long anticipated." No one could have forecasted the reduction in the rate of growth in demand for power in the CAPCO area after the Arab Oil Embargo or the regulatory problems occasioned by the incident involving the Babcock and Wilcox unit at Three Mile Island. The planning costs were incurred prudently, and the Ohio Court's refusal to allow at least re-

covery *of* those costs amounts to the same kind of confiscation as was found unconstitutional in *Pacific Gas, supra.*

Justice Brandeis, dissenting in *Pacific Gas,* found only issues of fact, and not law, in the case, and proposed that justice would be better served by adopting the "prudent investment" theory of rate base. In *Missouri ex rel Southwestern Bell Tel. Co. v. Pub. Serv. Comm.,* 262 U.S. 276, at 290, he had noted in his concurring opinion, that "The thing devoted by the investor to the public use is not specific property, tangible or intangible, but capital embarked in the enterprise." In his dissent in *Pacific Gas,* he expanded on that theme:

> "If a new device is adopted which involves additional investment (to buy a new plant or a patent right), the company's investment, on which the return must be paid, is increased by that amount. If the new device does not involve new investment, but the innovation involves increased current payments (like royalties for use of a process), the additional disbursement is borne by the community as an operating expense. The cost of a scrapped plant is *carried as part of the investment on which a return must be paid unless and until it has been retired,* — that is, *fully paid for,* out of the depreciation reserve. Thus, justice both to the owners of the utility and to the public is assured." (265 U.S. at 425, emphasis is added).

It is noteworthy that even Justice Brandeis in dissent made a point of requiring that a scrapped plant must be "fully paid for . . ." Under his "prudent investment" theory of rate base, cited with approval in *Hope,* Justice Brandeis expressly noted that the investor is entitled to a return *of* his investment in utility plant, whether or not the plant is "scrapped." That is all that The Cleveland Electric Illuminating Company is requesting here.

More recently the Court of Appeals for the District of Columbia has had occasion to address a similar question. In *Washington Gas Light Co., et al. v. Baker,* 188 F.2d 11 (D.C. Cir. 1950), *cert. den.* 340 U.S. 952 (1951), that court affirmed the District Court's reversal of a Utilities

Commission rate order which included the depreciated original cost of the utility's abandoned West Plant *in rate base* in determining the rates. By including the abandoned plant in rate base, the Commission in *Washington Gas Light* awarded a return *on* the investment in the abandoned plant. (The issue in the case at bar, the recovery *of* the investment, was not raised or decided regarding the West Plant.[8]) The Circuit Court found that the record before the Commission was inadequate for it to determine whether the investor had *already* been compensated for the risk of

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[8] *Washington Gas Light* involved the question of recovery *on* rate base, which was not requested or granted in the present case. Here, appellant only requested recovery *of* expenditures in cost of service. It is noteworthy that the *Washington Gas Light* case affirmed the Commission's allowance of a recovery *of* rate base investment by a ten year amortization in cost of service of "extraordinary" expenditures for converting customer's appliances from manufactured to natural gas *and* rate base treatment (a recovery *on* the investment) for the unamortized portion. The extraordinary conversion expenditures are obviously closely analogous to the planning expenditures in this case.

obsolescence through either depreciation expense in cost of service or "as a risk considered in fixing the permissible rate of return." (188 F.2d at 20). Accordingly, the decision of the Commission was vacated and remanded because it potentially had allowed the investor to recover compensation *on* his investment twice, once through depreciation accruals and again through the rate of return. The court commented that it seemed "likely . . . in view of the prevalence in the past of the doctrine that abandoned property would not be included in the rate base . . . that investors have been compensated for the risk of obsolescence." (188 F.2d at 20).

In the present case, it is undisputed that the investors were *not* compensated through depreciation expense or in the rate of return, for the risk that these planning, engineering, and initial construction costs would be entirely excluded from cost of service.

The reason here is precisely the converse of the assumption mentioned by the *Washington Gas Light Court*. Since "the overwhelming weight of authority from other jurisdictions supports the position of the [Ohio] commission" allowing recovery of such planning costs (67 Ohio St.2d at 162), CEI's investors did not anticipate the risk of exclusion from cost of service in Ohio and therefore did not cause the market to reflect that risk in a higher required rate of return. This is the uncontradicted evidence of record.

The undisputed evidence in this record met the standards of *Washington Gas Light* to qualify for not just a return *of* the investment, but also a return *on* the investment. Since the investor was not compensated through depreciation expense or through rate of return, the reasoning of *Washington Gas Light* clearly demonstrates that Ohio Revised Code § 4909.15(A)(4), as construed, simply confiscates the capital which appellant was required by law to dedicate to the present and future convenience of the ratepayers.

CONCLUSION

It is important to note that this appeal is *not* an attempt to persuade this Court to inject itself into an area entrusted to the expert discretion of a state regulatory agency. On the contrary, in this case the Supreme Court of Ohio has construed Ohio Revised Code § 4909.15(A)(4) to deprive the Ohio Public Utilities Commission of any discretion to apply the Ohio statutory rate-making formula to produce results that meet the *Bluefield* and *Hope* criteria. The Commission now cannot include certain prudent expenses in cost of service even though, as it found, it had not in past or even present rates compensated the investor by recognizing a higher overall rate of return as reasonable in light of this new and unforeseen degree of risk. The Commission has, under this decision, no discretion in the matter, and we are confronted with no evidentiary or technical ratemaking issues at all. Under Ohio Revised Code § 4909.15(A)(4), as construed below, the Public Utilities

Commission of Ohio *cannot*, by definition, meet the *Hope* requirement that it establish rates "which enable the company . . . to compensate its invesors for the risks assumed. . . ." (320 U.S. at 606).

The Public Utilities Commission allowed amortization of the planning costs as a cost of service and then found a fair and reasonable overall rate of return to be 10.82 percent. The Supreme Court of Ohio has now held that Ohio Revised Code § 4909.15(A)(4) prohibits the recovery of such planning expenses through rates and the Commission has now reduced appellant's rates by excluding the expenses attributable to the cancelled facilities. As a consequence, the rates have been established based on a cost of service which is artificially low, *without any change in the rate of return*, and the resulting rates inevitably yield an overall rate of return which *must* be below that which has been *found* to be fair, just and reasonable. Such rates, appellant submits, are confiscatory in violation of the Constitution.

For the foregoing reasons, the questions presented are so substantial as to require plenary consideration, with briefs on the merits and oral argument, for their resolution.

Respectfully submitted,

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EXHIBIT 1

Company/Unit	State or Jurisdiction	Cost (Million)	Type	Litigation
Rochester Gas & Electric/Sterling	New York State Public Service Commission (NYSPSC)	$23	Nuclear	Hearings pending with NYSPSC with current Rate Case pending outcome.
Long Island Light Co./James Port 1 & 2	New York Public Utility Commission	$39	Nuclear	Not yet claimed but proceedings to follow.
Jersey Central Power & Light Forked River	New Jersey Public Utility Commission	$4.2	Nuclear	Current proceeding with Public Utility Commission.
Mississippi Power and Light/Dasota County	Mississippi Public Utility Commission	$1.7	Coal	Will appeal to State Supreme Court on Commissions 70% allow. amortization decision.
New England Power Company/Salem (Harbon 5)	FERC	$12.5	Fossil-Oil	Issue of rate base and amortization before D.C. Court of Appeals (will appeal to Supreme if necessary).
New England Power Company/Montague 1 & 2	FERC		Nuclear	Not yet claimed but proceedings to follow.
Detroit Edison/ Greenwood 2 & 3	Michigan Public Utility Commission	$70	Nuclear	Case pending.
Niagara Mohawk Power Corp./ Sterling	New York State Public Service Commission (NYSPSC)	$23	Nuclear	Case pending with NYSPSC.
Central Hudson/ Sterling	New York State Public Service Commission (NYSPSC)		Nuclear	Case pending with NYSPSC.

EXHIBIT 1 (continued)

Company/Unit	State or Jurisdiction	Cost (Million)	Type	Litigation
Orange & Rockland Utilities Inc./ Sterling	New York State Public Service Commission (NYSPSC)	$14	Nuclear	Case pending with NYSPSC but rate case not postponed.
Wisconsin Power & Light/Koshkohong	Wisconsin Circuit Court	$7.0	Nuclear	Commission ruled in favor of amortization with Circuit Court now reviewing.
Central Maines Power/Richmond & Sears Island	Maine Public Utilities Commission	$3.5	Coal	In Appeals Court to review Maine Comm. Decision.
Northern States Power/Tyrone Energy Park 1	Wisconsin Public U.C. & FERC	$67	Nuclear	Appeals in District Court in N. Dakota and Minn.
Portland General Electric/Pebble Springs 1 & 2	Oregon Public Utilities Commission	$61	Nuclear	Plant cancelled at Oregon site, pending relocation; likely to sue for current costs.
Pudget Sound Power & Light/ Pebble Springs 1 & 2	Oregon Public Utilities Commission	$30	Nuclear	Plant cancelled at Oregon site, pending relocation; likely to sue for current costs.
Pacific Power and Light/Pebble Springs 1 & 2	Oregon Public Utilities Commission	$38	Nuclear	Plant cancelled at Oregon site, pending relocation; likely to sue for current costs.
Northern Indiana Public Service/ Bailey #1	Indiana Public Utilities Commission	$205	Nuclear	Plans cancelled, proceedings to follow.

Appendix

81-1002

Case No.

Office-Supreme Court, U.S.
FILED
NOV 25 1981
ALEXANDER L. STEVAS,
CLERK

In the Supreme Court of the United States

October Term, 1981

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

Appellant,

vs.

OFFICE OF CONSUMERS' COUNSEL, SENIOR CITIZENS COALITION, GREATER CLEVELAND WELFARE RIGHTS ORGANIZATION, INC., WESTERN RESERVE ALLIANCE, NORTH SHORE ALERT, CLEVELAND CHAPTER OF OHIOANS FOR UTILITY REFORM,

and

THE PUBLIC UTILITIES COMMISSION OF OHIO,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF OHIO

APPENDIX

Of Counsel:

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INDEX TO APPENDIX

	PAGE
Decisions of the Supreme Court of Ohio Denying Rehearing (filed September 1, 1981)	A-1, A-2, A-3
Mandates of the Supreme Court of Ohio (filed September 3, 1981)	B-1, B-2, B-3
Decision and Opinion of the Supreme Court of Ohio (filed July 15, 1981)	C-1
Decision and Opinion of the Public Utilities Commission of Ohio (filed July 10, 1980)	D-1
Appellant's Notice of Appeal To The Supreme Court of the United States (filed September 2, 1981)	E-1
Ohio Statutes: Ohio Revised Code §§ 4905.02, 4905.03, 4905.04, 4905.05, 4905.06, 4905.22, 4909.15, 4909.18, 4909.19, 4909.43; Ohio Administrative Code § 4901:1-9-05; Ohio Supreme Court Rule IX, Section 1 and 2	F-1

APPENDIX A-1

DECISIONS OF THE SUPREME COURT OF OHIO DENYING REHEARING

(Filed September 1, 1981)

THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO, City of Columbus. } 1981 Term To wit: September 1, 1981

CITY OF CLEVELAND, *Appellant,*

vs.

PUBLIC UTILITIES COMMISSION OF OHIO et al., *Appellees.*

No. 80-1547 REHEARING

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. .... Page ....

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 1st day of September, 1981.

THOMAS L. STARTZMAN,
Clerk.

By .....,
Deputy.

APPENDIX A-2

DECISIONS OF THE SUPREME COURT OF OHIO DENYING REHEARING

(Filed September 1, 1981)

THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO,
CITY OF COLUMBUS.
} 1981 Term
To wit: September 1, 1981

SENIOR CITIZENS COALITION et al.,
Appellants,
vs.
PUBLIC UTILITIES COMMISSION OF OHIO et al.,
Appellees.
} No. 80-1528 REHEARING

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. .... Page ....

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 1st day of September, 1981.

THOMAS L. STARTZMAN,
Clerk.

By .....,
Deputy.

APPENDIX A-3

DECISIONS OF THE SUPREME COURT OF OHIO DENYING REHEARING

(Filed September 1, 1981)

THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO,
CITY OF COLUMBUS.

1981 Term
To wit: September 1, 1981

OFFICE OF CONSUMERS' COUNSEL,
Appellant,
vs.
PUBLIC UTILITIES COMMISSION OF OHIO et al.,
Appellees.

No. 80-1480
REHEARING

It is ordered by the court that rehearing in this case is denied.

I, THOMAS L. STARTZMAN, Clerk of the Supreme Court of the State of Ohio, do hereby certify that the foregoing entry was correctly copied from the records of said Court, to wit, from Journal No. .... Page ....

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of the Supreme Court this 1st day of September, 1981.

THOMAS L. STARTZMAN,
Clerk.

By .....,
Deputy.

APPENDIX B-1

MANDATE OF THE SUPREME COURT OF OHIO

(Filed September 3, 1981)

THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO, } 1981 Term
CITY OF COLUMBUS. } To wit: July 15, 1981

OFFICE OF CONSUMERS' COUNSEL,
Appellant,
vs.
PUBLIC UTILITIES COMMISSION OF OHIO et al.,
Appellees.

No. 80-1480
MANDATE

To the Honorable PUBLIC UTILITIES COMMISSION OF OHIO, within and for the County of Franklin, Ohio, Greeting:

The Supreme Court of Ohio commands you to proceed without delay to carry the following judgment in this cause into execution:

Order of the Public Utilities Commission reversed in part and affirmed in part and cause remanded to the Commission, for the reasons set forth in the opinion rendered herein.

THOMAS L. STARTZMAN,
Clerk

September 3, 1981

THOMAS L. STARTZMAN

SAM K. ADKINS, *Deputy*

RECORD OF COSTS

Docket Fee ..... $20.00 Paid by Office of Consumers' Counsel

APPENDIX B-2

MANDATE OF THE SUPREME COURT OF OHIO
(Filed September 3, 1981)

THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO, } 1981 Term
CITY OF COLUMBUS. } To wit: July 15, 1981

SENIOR CITIZENS COALITION et al.,
Appellants,
vs.
PUBLIC UTILITIES COMMISSION OF OHIO et al.,
Appellees.

No. 80-1528
MANDATE

To the Honorable PUBLIC UTILITIES COMMISSION OF OHIO, within and for the County of Franklin, Ohio, Greeting:

The Supreme Court of Ohio commands you to proceed without delay to carry the following judgment in this cause into execution:

Order of the Public Utilities Commission reversed in part and affirmed in part and cause remanded to the Commission, for the reasons set forth in the opinion rendered herein.

THOMAS L. STARTZMAN,
Clerk

September 3, 1981

THOMAS L. STARTZMAN

SAM K. ADKINS, *Deputy*

RECORD OF COSTS

Docket Fee ..... $20.00 Paid by Joseph P. Meissner

APPENDIX B-3

MANDATE OF THE SUPREME COURT OF OHIO
(Filed September 3, 1981)

THE SUPREME COURT OF THE STATE OF OHIO

THE STATE OF OHIO, City of Columbus. } 1981 Term
To wit: July 15, 1981

CITY OF CLEVELAND
Appellant,

vs.

PUBLIC UTILITIES COMMISSION OF OHIO et al.,
Appellees.

No. 80-1547
MANDATE

To the Honorable PUBLIC UTILITIES COMMISSION OF OHIO, within and for the County of Franklin, Ohio, Greeting:

The Supreme Court of Ohio commands you to proceed without delay to carry the following judgment in this cause into execution:

Order of the Public Utilities Commission affirmed in part and reversed in part and cause remanded to the Commission, for the reasons set forth in the opinion rendered herein.

THOMAS L. STARTZMAN,
Clerk

September 3, 1981

THOMAS L. STARTZMAN,

SAM K. ADKINS, *Deputy*

RECORD OF COSTS

Docket Fee ..... $20.00 Paid by City of Cleveland

APPENDIX C

DECISION AND OPINION OF THE SUPREME COURT OF OHIO

(Filed July 15, 1981)

Statement of the Case.

OFFICE OF CONSUMERS' COUNSEL, APPELLANT, *v.*
PUBLIC UTILITIES COMMISSION OF OHIO ET AL., APPELLEES.

SENIOR CITIZENS COALITION ET AL., APPELLANTS, *v.*
PUBLIC UTILITIES COMMISSION OF OHIO ET AL., APPELLEES.

CITY OF CLEVELAND, APPELLANT, *v.*
PUBLIC UTILITIES COMMISSION OF OHIO ET AL., APPELLEES.

[Cite as Consumers' Counsel v. Pub. Util. Comm. (1981), 67 Ohio St. 2d 153.]

Public Utilities Commission—Electric companies—Rate increase—Allowable operating expenses—Amortization of cost of terminated nuclear facilities, unlawful.

The Public Utilities Commission's treatment of a utility's investment in terminated nuclear generating stations as amortizable costs to be recovered from the utility's ratepayers is inconsistent with the ratemaking formula contained in R. C. 4909.15 and is unreasonable and unlawful.

(Nos. 80-1480, 80-1528 & 80-1547—
Decided July 15, 1981.)

APPEALS from the Public Utilities Commission of Ohio.

These three cases are appeals taken from an order of appellee, Public Utilities Commission of Ohio (hereinafter "commission"), granting intervening appellee, the Cleveland Electric Illuminating Company (hereinafter "CEI"), a rate increase of approximately $69.6 million. The commis-

sion order further provided for the amortization over a ten-year period of CEI's substantial investment in four terminated nuclear power plants.[1]

The commission's order dealt with two cases that had been consolidated. Case No. 79-537-EL-AIR involved CEI's application to increase rates. Case No. 79-744-EL-CMR concerned a complaint and appeal taken by CEI from a 1979 rate setting ordinance passed by the City of Cleveland.

Inasmuch as these three appeals primarily concern issues relating to the nuclear power plant cancellations, we shall briefly reprise the history of these now terminated facilities. In 1967, CEI joined with four other electric companies to form the Central Area Power Coordination Group (CAPCO).[2] The CAPCO companies sought to achieve economies of scale and greater service reliability by jointly planning, constructing, and operating electrical generating facilities. In 1973, the CAPCO group committed itself to build the four nuclear plants at issue herein based on forecasts that predicted a substantially increased demand for electricity by the CAPCO companies' customers during the 1970's and 1980's. These forecasts subsequently had to be revised downward when increasing energy costs spurred conservation efforts and significantly softened the demand for electricity. Moreover, the 1979 accident at Three Mile Island prompted the Nuclear Regulatory Commission to issue stringent and costly new standards for nuclear power plants, requiring major design changes in the Babcock and Wilcox units that CAPCO planned to construct and oper-

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[1] Davis-Besse Units 2 and 3 and Erie Units 1 and 2 are the cancelled facilities at issue.

[2] In addition to CEI the CAPCO group consists of Toledo Edison, Ohio Edison, and two Pennsylvania utilities, Duquesne Light Co. and Pennsylvania Power Co.

ate. After much study and redesign the CAPCO companies decided to terminate the four units on January 23, 1980. When the decision to cancel the plants was announced, CAPCO had already invested considerable sums in the projects. Preliminary expenses included expenditures for engineering, siting, environmental, geological, and seismic studies, and for obtaining state and federal licenses. Moreover, to comply with detailed regulatory requirements and complete all the necessary documents, certain plant components had to be purchased at a fairly early stage in the planning process. CEI's share of the total CAPCO investments in the four cancelled plants amounted to approximately $56,400,000 as of the date of termination.

The instant CEI rate case was pending before the commission when the plant terminations were announced.[3] The commission had accepted CEI's application for a rate increase as of September 17, 1979, and had established calendar year 1979 as the test year and June 30, 1979, as the date certain. The commission staff conducted an investigation and issued its initial report in March 1980. This report did not make reference to the terminated nuclear plants because CEI did not officially inform the commission of the plant cancellations until February 1980. The commission staff, at appellants' request, then conducted a supplemental investigation to consider the effect of the terminated plant expenditures on CEI's rate application. The staff completed its investigation of the cancelled nuclear facilities and filed revised schedules in mid-April. The staff recommended that the investment in the four nuclear plants should be amortized over a ten-year period as CEI had requested.

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[3] The rates established by the commission order in the instant ratemaking case have recently been superseded by new rates set by order on May 4, 1981 in case No. 80-376-EL-AIR.

Opinion, per SWEENEY, J.

Public hearings on the rate increase application began on April 2, 1980, and continued for 32 days. Staff witnesses appeared and testified at the hearings in regard to the cancelled nuclear plants and other matters contained in the application. Appellants were represented at, and participated fully in, these public hearings.

The commission issued its order on July 10, 1980. Appellants timely filed for a rehearing which the commission denied as to the issues raised in the present appeal.

These causes are now before this court upon appeals as of right.

Mr. William A. Spratley, consumers' counsel, *Mr. Gary M. Petroff* and *Mrs. Gretchen J. Hummel,* for appellant Consumers' Counsel.

Mr. Joseph P. Meissner, for appellants Senior Citizens Coalition *et al.*

Mr. Thomas E. Wagner, director of law, and *Mr. Craig A. Glazer,* for appellent City of Cleveland.

Mr. William J. Brown, attorney general, *Mr. Marvin I. Resnik* and *Mr. David M. Neubauer,* for appellee Public Utilities Commission.

Mr. Alan D. Wright, Mr. Craig I. Smith, Messrs. Squire, Sanders & Dempsey, Mr. Alan P. Buchmann, Mr. Lowell L. Garrett, Mr. William C. Donahue and *Mr. Richard W. McLaren, Jr.,* for intervenor-appellee The Cleveland Electric Illuminating Co.

SWEENEY, J. The scope of this court's review of commission orders is set forth in R. C. 4903.13, which states in pertinent part:

"A final order made by the public utilities commission shall be reversed, vacated, or modified by the supreme court on appeal, if, upon consideration of the record, such

court is of the opinion that such order was unlawful or unreasonable."

"Under the 'unlawful or unreasonable' standard specified in R. C. 4903.13, this court will not reverse or modify an opinion and order of the Public Utilities Commission where the record contains sufficient probative evidence to show that the commission's determination is not manifestly against the weight of the evidence and is not so clearly unsupported by the record as to show misapprehension, mistake or willful disregard of duty," *Columbus v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 103, 104. See, also, *Consumers' Counsel v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 108, 110; *Ohio Utilities Co. v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 153, 164; *Duff v. Pub. Util. Comm.* (1978), 56 Ohio St. 2d 367, 370; *General Motors Corp. v. Pub. Util. Comm.* (1976), 47 Ohio St. 2d 58, paragraph two of the syllabus; *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.* (1975), 42 Ohio St. 2d 403, paragraph eight of the syllabus. We assess the appellants' objections with this standard of review in mind.

I A.

In its order the commission allowed approximately $91 million to be included in the rate base for construction work in progress (CWIP) pursuant to R. C. 4909.15(A)(1) and 4909.15(E). R. C. 4909.15(A)(1) states in relevant part:

"***The commission may, in its discretion, permit a reasonable allowance for construction work in progress but, in no event, may any allowance for construction work in progress be made by the commission until it is determined, after a physical inspection, that the particular construction project is a least seventy-five per cent complete."

R. C. 4909.15(E) imposes the following limitation on allowable CWIP:

Opinion, per SWEENEY, J.

"In no event shall an allowance for construction work in progress under division (A)(1) of this section exceed twenty per cent of the total valuation as stated in such division, not including such allowance."

Some $90 million of the CWIP allowance was directly attributable to the Bruce Mansfield coal-fired generating station, which came on line several months after the new rates became effective. It is unquestioned that Bruce Mansfield met the 75 percent completion criterion for rate base eligibility pursuant to R. C. 4909.15(A)(1). Moreover, it is uncontroverted that inclusion of the Bruce Mansfield-related CWIP did not exceed the 20 percent of total valuation limitation imposed by R. C. 4909.15(E).

I A(i).

Appellants Senior Citizens Coalition et al. (hereinafter "SCC"), in case No. 80-1528, challenge the commission's allowance for CWIP in this case on the basis that the CWIP provisions contained in R. C. 4909.15(A)(1) represent an unconstitutional delegation of legislative power. Specifically, SCC contends that the statute "***establishes no definite policy nor provides any standard for the exercise of PUCO discretion in permitting an allowance for construction work in progress and***therefore the PUCO should be prohibited from granting any such allowance.***"

We find no merit in SCC's constitutional challenge to the CWIP provisions because the commission's discretion is sufficiently circumscribed by the specific eligibility criteria enumerated in the statute. As we stated in *Consumers' Counsel v. Pub. Util. Comm., supra* (58 Ohio St. 2d 108), at page 113:

"***We believe these limitations adequately confine commission discretion. Further restriction would conceivably hinder the flexibility necessary to enable the com-

mission to carry out legislative will. For these reasons, this court holds that the discretion granted the commission under R. C. 4909.15 to authorize a reasonable allowance for construction work in progress in a utility's rate base constitutes a lawful delegation of the state's police power by the General Assembly."

We expressed the same view of the CWIP provisions of R. C. 4909.15(A)(1) in *Cleveland v. Public Util. Comm.* (1980), 63 Ohio St. 2d 62, 68. In the case at bar we decline to strike down the CWIP statute as an unconstitutional delegation of legislative authority.

I A(ii)

Both SCC and appellant City of Cleveland, in case No. 80-1547, contend that the inclusion of a CWIP allowance in this case constituted an abuse of commission discretion. As previously noted, the Bruce Mansfield generating station, which accounted for virtually all of the CWIP at issue, met the 75 percent completion criterion and came on line several months after the new rates went into effect. Under these circumstances, we cannot say that the commission's decision was either manifestly against the weight of the evidence or supported by the record. *Columbus vs. Pub. Util. Comm., supra.* Therefore, we refuse to disturb the commission's findings on the propriety of including a CWIP allowance in CEI's rate base. Accordingly, we reject appellants' assertions that the commission abused its discretion in granting the CWIP allowance.

II.

SCC alleges that the commission did not adequately investigate CEI's generating capacity to determine whether the utility had excess capacity. The commission staff investigated CEI's generating capacity and determined that

the reserve capacity was adequate but not excessive.[4] Staff and CEI witnesses testified to the same effect at the hearings before the commission wherein they explained the methodology by which they reached their conclusions.

We have in a previous case acknowledged the difficulties the commission and utilities face on the excess capacity issue.

"* * *Since utilities must anticipate load growth years in advance to maintain adequate capacity to ensure reliable service, it is unrealistic to expect a utility to have only the precise amount of capacity needed at a given time." *Cleveland v. Pub. Util. Comm., supra,* at 65. To paraphrase what we stated in *Consumers' Counsel v. Pub. Util. Comm.* (1980), 64 Ohio St. 2d 71, 79: Limited judicial review of an excess capacity determination is sound for the reason that while excess capacity analyses have an aura of precision about them, they are fraught with judgments and assumptions. Given the inherent problems of accurately projecting load growth, we are satisfied that the commission's excess capacity methodology is reasonable and that the factual findings are supported by the record. SCC's challenge on the question of excess capacity is, therefore, without merit.

III A.

Before proceeding to the merits of appellants' contentions on the question of whether the commission lawfully and reasonably treated the four cancelled nuclear power plants as amortizable costs, we must first consider two procedural issues raised by appellant Cleveland in case No. 80-1547. Cleveland first contends that CEI violated the

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[4] The record indicates that CEI had available 3,469 megawatts (MW) of capacity. The 1979 peak load was 3,097 MW and the forecasted 1980 peak load was 3,450 MW.

notice provisions of R. C. 4909.18 and 4909.19 R. C. 4909.18(E) requires that "[a] proposed notice for newspaper publication fully disclosing the substance of the application" must accompany the rate increase application. R. C. 4909.19 requires the applicant to publish in newspapers of general circulation the "substance and prayer of its application."[5] Cleveland asserts that CEI's proposed notice under R. C. 4909.18 and its published notice under R. C. 4909.19 were inadequate because no mention was made of the four terminated nuclear units in either notice.

Cleveland relies on *Committee Against MRT v. Pub. Util. Comm.* (1977), 52 Ohio St. 2d 231, and *Ohio Assn. of Realtors v. Pub. Util. Comm.* (1978), 60 Ohio St. 2d 172, to support its contention that CEI's statutory notices were inadequate. In *MRT, supra,* we stated, at page 233, that "***a highly innovative and material change in the *method of charging* customers should be included in the notice." (Emphasis added.) The cancelled power plant information that Cleveland insists should have been included in the CEI notices herein complained of did not relate to an innovative method of charging that would profoundly affect the rates paid by certain categories of utility customers. Therefore, Cleveland's reliance on *MRT* and *Realtors* is misplaced.

The proposed notice under R. C. 4909.18(E) need only convey the "substance" of the application and the notice published pursuant to R.C. 4909.19 need only contain the "substance and prayer" of the application. The decision of the CAPCO companies to terminate the pro-

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[5] Appellees challenge Cleveland's standing to complain of the allegedly flawed notices. The standing question, however, was not raised before the commission and, therefore, according to our well-settled rule, the issue is not properly before this court. *Stores Realty Co. v. Cleveland* (1975), 41 Ohio St. 2d 41, 43.

posed plants did not alter the "substance" or the "substance and prayer" of CEI's application because CEI did not request additional rate relief when it revised its original application to reflect the terminated plant expenditures. We hold that the CEI notices met the standards of R. C. 4909.18 and 4909.19, and consequently Cleveland's assertions to the contrary are unfounded.

III B.

Cleveland's second procedural objection relates to the adequacy of the staff investigation and report in regard to the cancelled nuclear power plants. R. C. 4909.19 requires that the commission investigate and issue a report on rate increase applications. The commission did conduct an investigation and prepared a report on the original CEI application. As noted however, the initial commission staff report was silent on the subject of the terminated plants because the decision to cancel the plants was announced too late to be included in the report. However, the staff did subsequently investigate the matter of the terminated facilities and assessed the effect of the cancelled generating stations on CEI's pending rate application. Cleveland now complains that the omission of these matters from the original report and the tardy presentation of the staff review of the four terminated plants after hearings on the application had already begun were prejudicial and in violation of R. C. 4909.19. Cleveland asserts that "intervenors have been consistently denied the opportunity to adequately prepare their case. They have [had] no opportunity to review the Staff's findings prior to hearings and thus no opportunity to prepare evidence to support or rebut the same."

Notwithstanding these contentions, Cleveland, after posing objections to the original report, did receive the benefits of the staff's investigation of the four terminated nuclear plants and had ample opportunity to cross-examine the commission's and CEI's experts at the public hearings. Cleveland did not seek additional time to prepare its case while these matters were pending before the commission. Moreover, Cleveland had already intervened in the case before the plant closing issue surfaced and therefore was not prejudiced by the omission of the cancelled plant data in the original report. *Worthington Hills Civic Assn. v. Pub. Util. Comm.* (1976), 45 Ohio St. 2d 11.

The purpose of the staff report is "***to facilitate meaningful contest of rate increase applications by providing interested parties with the materials necessary for an informed challenge." *Duff v. Pub. Util. Comm.* (1978), 56 Ohio St. 2d 367, 376. The commission report in this case, as supplemented by the follow-up investigation conducted by the commission staff, provided appellant Cleveland with the opportunity to make an informed challenge. Therefore, the commission's investigation and report in the instant rate application case comply with the statutory requirements set forth in R. C. 4909.19.

IV A.

The core issue in each of these appeals is whether the commission lawfully and reasonably permitted CEI to treat its investment in the four cancelled nuclear generating stations as amortizable costs.

The commission order stated and analyzed the question in this fashion.

"***What the company seeks is the recovery of costs incurred on behalf of its ratepayers to assure that adequate service could be maintained***. The significant question,

given the Commission's past pronouncements with respect to the impropriety of the recovery of past losses through future rates, is whether the amortization of these extraordinary costs does violence to this principle. The distinguishing feature that sets this adjustment apart from those we have rejected on this ground in the past is that costs associated with the termination of the units did not really become costs until the fact of termination. Cancellation does not create a past loss, but gives rise to a current cost.***[R]ejection of this adjustment would have a very direct impact on applicant's final performance as, in the absence of funding of the amortization through rates, applicant would be required to write off these costs currently***. Thus, we now see the wisdom of the standard emerging from the cases from other jurisdictions; if the expenditures are prudent, amortization should be permitted.

"In determining whether these expenditures were prudent, one must bear in mind what is and what is not at issue. No one disputes that the 1973 decision to embark on the construction in question was reasonable as it was based on the best data available***. Similarly, no one disputes that the decision to terminate construction was reasonable, given the intervening decline in growth expectations and the uncertainties which now attend the construction of nuclear units.***The Commission finds that applicant's decisions were reasonable and prudent at every step of this process, and concludes that the proposed adjustment should be approved."

The appellants argue that the commission exceeded its authority and disregarded a carefully crafted statutory scheme when it acceded to CEI's request to amortize the cancelled nuclear plant expenditures.

There is no question but that the overwhelming weight of authority from other jurisdictions supports the

position of the commission.[6] In only two instances has amortization been disallowed.[7] It is important to note, however, that none of the previous rulings on this precise issue represents the opinion of the highest court of the jurisdiction in which the case arose. Virtually all of the decisions that the commission, CEI, and the *amici* cite in support of amortization derive from regulatory proceedings. Even more significant is the fact that no other case has considered the propriety of the commission's proposed amortization with reference to Ohio law. Thus, while counsel for the parties and intervenors before the court in this cause have thoroughly canvassed the administrative decisions in other jurisdictions and have supplied this court with copies of those decisions, we must regard these foreign regulatory opinions as advisory in nature. The construction of Ohio law is particularly the province of this court, and we are nowise bound by the pronouncements of regulatory regimes elsewhere in effect.

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[6] See, *e.g.*, *Re San Diego Gas & Electric Co.* (Cal. Pub. Util. Comm. 1979), 29 P.U.R. 4th 613; *Re Potomac Electric Power Co.* (Md. Pub. Ser. Comm. 1977), Order No. 6999; *Re Consumer Power Co.* (Mich. Pub. Ser. Comm. 1975), Case No. F-700; *Re Northern States Power Co.* (Minn. Pub. Ser. Comm. 1977), Dkt. E-0021 GR-76-934; *Re Public Service Electric and Gas Co.* (N.J. Dept. of Energy, Bd. of Pub. Util. 1980), Dkt. No. 794-310; *Re Consolidated Edison Co. of New York* (N.Y. Pub. Ser. Comm.), Case No. 9187; *Re Carolina Power & Light Co.* (N.C. Util. Comm. 1979), Dkt. No. E-2, Sub. 352; *Re Gulf States Utilities Co.* (Pub. Util. Comm. of Texas 1979), Dkt. No. 2677; *Re Virginia Electric & Power Co.* (Va. Corp. Comm. 1979), 29 P.U.R. 4th 65; *Re Wisconsin Electric Power Co.* (Pub. Ser. Comm. of Wis. 1980), Case No. 05-C1-3; *Re Potomac Electric Power Co.* (D.C. Pub. Ser. Comm. 1979), 29 P.U.R. 4th 517.

[7] See *Re Arizona Public Service Co.* (Ariz. Corp. Comm. 1980), Decision No. 51009; *Re Northern States Power Co.* (Pub. Ser. Comm. of N.D. 1980), Case No. 10,097.

Opinion, per SWEENEY, J.

IV B.

The commission's approval of amortization was predicated on the prudence of CEI's original decision to build the nuclear facilities and the subsequent decision to cancel the plants. We must decide whether the test of prudence, as applied by the commission, which supports treating the expenditures associated with the terminated nuclear generating stations as amortizable costs, is consistent with the statutorily mandated ratemaking formula contained in R. C. 4909.15.

IV B(i).

The controversy surrounding the cancelled nuclear power plants focuses primarily on R. C. 4909.15(A)(4), which delineates the service-related costs that a utility may recover from its ratepayers. This section states in relevant part:

"The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:

"***

"(4) The cost to the utility of rendering the public utility service for the test period***"

The commission urges that "an expenditure by a utility can be considered a cost of rendering the public utility service if it fails in fact to achieve its intended purpose*** [if] the expense was reasonably calculated to provide [future] utility service at a reasonable cost." The underpinnings for the commission rationale may be found in those statutory provisions that require utilities to maintain adequate service presently and for the foreseeable future. See, *e.g.*, R. C. 4905.22 (adequate service and facilities).

Notwithstanding the provisions that impose a duty on utility companies to plan for the future, the question under

R. C. 4909.15(A)(4) remains whether the cancelled plant expenditures represent "[t]he cost to the utility of rendering the public utility service for the test period." Test period considerations aside, what the company sought and what the commission granted was the amortization as service-related costs of an investment that never provided any service whatsoever to the utility's customers.

We seriously question whether the General Assembly contemplated that the commission would treat the type of expenditures controverted herein as costs under R. C. 4909.15(A)(4). The now terminated nuclear plants represented a major capital investment that ultimately would have been included in the rate base under R. C. 4909.15 (A)(1), had the projects not been cancelled. It is our opinion that R. C. 4909.15(A)(4) is designed to take into account the normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period.[8] A non-exhaustive list of such expenses would include reasonable expenditures for repairs, maintenance, personnel-related costs, administrative expenses, and taxes.

The extraordinary loss sustained by CEI in connection with the terminated nuclear plants cannot be transformed into an ordinary operating expense pursuant to R. C. 4909.15(A)(4) by commission fiat. The commission's statement that "[c]ancellation does not create a past loss, but gives rise to a current cost" is unpersuasive. Under this rationale we question whether there could ever be a "past loss" the return of which would not be recoverable in future ratemaking proceedings notwithstanding the com-

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[8] Appellants contend that the "direct, primary benefit" test enunciated in *Cleveland* v. *Pub. Util. Comm.* (63 Ohio St. 2d 62), *supra*, is applicable to the case at bar. We disagree. The direct, primary benefit standard should not be wrenched from the institutional advertising expenses and charitable contributions context in which it arose.

mission's assertion to the contrary. The commission's characterization of the investment in the four terminated plants as "cost" under R. C. 4909.15(A)(4) in light of what we perceive to be the legislative intention underlying that section is unreasonable. Therefore, to the extent that the commission's order in regard to the cancelled plants is predicated on R. C. 4909.15(A)(4), the order cannot stand.

IV B(ii).

The commission and CEI also argue that even if, as we have found, R. C. 4909.15(A)(4) is inapplicable, then under R. C. 4909.15(D)(2)(b) the commission may authorize the amortization of the investment in the terminated nuclear facilities.

R. C. 4909.15 states in relevant part:

"(D) When the public utilities commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section***that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

"***

"(2) With due regard to all such other matters as are proper, according to the facts in each case,

"***

"(b)***fix and determine the just and reasonable rate, fare, charge, toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one.***"

Opinion, per SWEENEY, J.

For purposes of R. C. 4909.15(D)(2)(b) the question presented is whether the cancelled nuclear power plant costs fall under the "all such matters as are proper" language of the statute. The commission views R. C. 4909.15(D)(2)(b) as a virtual wild card to be played whenever the commission in its discretion sees fit. We interpret the statute less sweepingly, first because the provisions are linked inextricably with the ratemaking factors contained in R. C. 4909.15(A) and (B), and secondly because the General Assembly undoubtedly did not intend to build into its recently revised (1976) ratemaking formula a means by which the commission may effortlessly abrogate that very formula.

To be a proper matter giving rise to a permissible adjustment under R. C. 4909.15(D)(2)(b), the matter in question must relate to factors otherwise included in R. C. 4909.15. R. C. 4909.15(D)(2)(b) makes reference to "the allowable *gross* annual revenues under division (B)." (Emphasis added.) Having previously determined that the nuclear plant costs are not properly includable under R. C. 4909.15(A), then these costs can have no effect on the gross annual revenue determination under R. C. 4909.15(B). Therefore, we reject the commission's argument invoking R. C. 4909.15(D)(2)(b) as alternative statutory authority for its order granting CEI permission to amortize its investment in the cancelled nuclear facilities.

It is our view that R. C. 4909.15(D)(2)(b) is designed to allow the commission to make minor adjustments to rates ascertained by the statutory formula when the criteria upon which the rates are based are skewed for one reason or another. Thus, under R. C. 4909.15(D)(2)(b), the commission may smooth out anomalies in the ratemaking equation that tend to make the test year data unrepresentative for ratemaking purposes.

Opinion, per SWEENEY, J.

IV B(iii)

"[T]his court has consistently recognized that the Public Utilities Commission is a creature of the General Assembly and may exercise no jurisdiction beyond that conferred by statute." *Dayton Communications Corp. v. Pub. Util. Comm.* (1980), 64 Ohio St. 2d 302, 307. See, also, *Werlin Corp. v. Pub. Util. Comm.* (1978), 53 Ohio St. 2d 76, 80; *Ohio Public Interest Group v. Pub. Util. Comm.* (1975), 43 Ohio St. 2d 175, 176, paragraph five of the syllabus; *Penn Central Transportation Co. v. Pub. Util. Comm.* (1973), 35 Ohio St. 2d 97, paragraph one of the syllabus. Stated differently, the commission may not legislate in its own right. This, however, is what the commission has attempted to accomplish in the case at bar.

The commission order engrafts upon the statutory ratemaking scheme an exception that would allow utility companies to recover their investment in unfinished projects ineligible for rate base treatment if the original decision to build the facilities and the subsequent decision to cancel the projects are prudent under the circumstances. In so doing the commission has exceeded its statutory mandate. We hold that the commission unreasonably and unlawfully exceeded its statutory authority when it approved amortization of CEI's investment in the four terminated nuclear power plants.

IV C.

Appellants contend that the commission also erred in including the cancelled plant costs in the calendar year 1979 test period because the termination was not announced until January 23, 1980. Inasmuch as we have already determined that the commission improperly allowed amortization of the utility's investment in the terminated nuclear facilities, it is unnecessary for us to address the timing issue raised in this cause.

Opinion, per SWEENEY, J.

IV D.

We are mindful of the policy considerations that prompted the commission's decision. The commission, CEI, and the *amici* argue strenuously that to rule as we have today will seriously disadvantage Ohio utilities in capital markets thereby "dri[ving] up the return on investment required by investors in Ohio utilities." This gloomy scenario, however, does not imbue the commission with the authority to rewrite the statutes. The statutes in question contain no provisions insulating investors from the type of losses sustained in the cancelled-plants venture.

If, as has been argued, these are parlous times for the utilities industry, and if, therefore, in order to attract and retain investment capital, utility companies must not only be granted a fair and reasonable rate of return pursuant to statute but must also be assured the return of capital invested in failed projects that would otherwise not be recoverable under the ratemaking formula, then the commission and the utilities should petition the General Assembly to enact changes in the ratemaking structure so as to provide this extra modicum of protection for the investors. Absent such explicit statutory authorization, however, the commission may not benefit the investors by guaranteeing the full return of their capital at the expense of the ratepayers. Under the ratemaking formula now in effect consumers are not chargeable for utility investments and expenditures that are neither included in the rate base nor properly categorized as costs. What we previously stated in a rate base case is applicable to the case at bar: "***It is only proper that their [the investors] venture be found operational before they commence to recoup their capital outlays from the consumers." *Consumers' Counsel v. Pub. Util. Comm.* (1979), 58 Ohio St. 2d 449, 456-457.

Concurring and Dissenting Opinion, per P. BROWN, J.

We take a dimmer view of the second policy argument advanced by the commission to support its order. The commission suggests that if the appellants prevail on this issue, then "[r]ather than prudently cancel certain projects, it is not inconceivable that at least some utility managements would complete expenditures on a project and have ratepayers pay a return on dollars which would have more wisely not been spent." R. C. 4909.154 specifically empowers the commission to investigate management policies, practices and organization to determine whether a public utility is properly managed. If a utility completes a project that should have been abandoned, then the commission must under the "used and useful" requirement of R. C. 4909.15(A)(1) disallow rate base treatment and under R. C. 4909.154 disallow any claimed operating expenses related to the unnecessary project. We are confident that if any utility managers who might be tempted to act as the commission suggests are aware that the commission, pursuant to its statutory responsibilities, is vigorously scrutinizing all proposed and in-progress construction projects, these managers will decide whether or not to abandon a particular project according to their best and most prudent business judgment. Thus, we reject the commission's argument that our decision today may engender imprudent decision making in utility company boardrooms.

For reasons hereinbefore stated the order of the commission is affirmed in part and reversed in part, and this cause is remanded to the commission for a redetermination of CEI's allowable operating expenses, excluding therefrom the expenditures attributable to the cancelled nuclear facilities.

Order reversed in part and affirmed in part.

Concurring and Dissenting Opinion, per P. BROWN, J.

CELEBREZZE, C. J., W. BROWN and C. BROWN, JJ., concur.

P. BROWN, LOCHER and HOLMES, JJ., concur in part and dissent in part.

PAUL W. BROWN, J., concurring in part and dissenting in part.

I concur in Parts I, II and III of the majority opinion insofar as they affirm the commission's decision to allow rate base treatment for CWIP attributable to the Bruce Mansfield coal-fired generating station. I dissent, however from Part IV of the opinion.

In Part IV of its opinion, the majority reverses the commission's decision to allow amortization of the costs incident to termination of the four nuclear facilities in question. In so doing, the majority does not disturb the commission's findings that CEI acted both prudently and reasonably in incurring these costs. Instead, the majority holds that it was not the intent of the General Assembly to treat expenditures of this type as "costs" within the meaning of R. C. 4909.15(A)(4). I believe the majority's interpretation of this section to be too restrictive.

The term "cost" is not defined in R. C. Chapter 4909. Therefore, it is necessary to look elsewhere to ascertain the meaning of this word. In 1961, the commission adopted standard accounting procedures to be used by Ohio utilities. "The system of accounts and records identified and designated as 'Uniform System of Accounts Prescribed for Public Utilities and Licensees effective January 1, 1961' * * * is adopted by this Commission * * *." Ohio Adm. Code 4901:1-9-05. This "Uniform System of Accounts" was promulgated in 18 C.F.R., Part 101.

An analysis of this uniform system clearly demonstrates that expenditures such as those incurred in the termination of the four nuclear generating units were in-

tended to fall within the statutory definition of "costs." The uniform system states, in part:

182 Extraordinary property losses.

"A. * * * this account shall include extraordinary losses on property *abandoned* or otherwise retired from service which are not provided for by the accumulated provisions for depreciation or amortization and which could not reasonably have been foreseen and provided for ***." (Emphasis added.) *Id.*, at 324.

"407 Amortization of property losses.

"This account shall be charged with amounts credited to account 182***." *Id.*, at 356.

This accounting system has been in effect in Ohio for approximately two decades. Given this fact, we can reasonably assume that the General Assembly was cognizant of its existence when it amended R. C. 4909.15 in 1976, and that it was not the intent of the General Assembly to treat these extraordinary property losses in a different manner in which they were treated by the Public Utilities Commission.

Moreover, as the majority correctly notes, "the overwhelming weight of authority from other jurisdictions supports the position of the commission." The majority dismisses this significant point with the facile statement that none of the cases from these other jurisdictions represents the opinion of the highest court of the jurisdiction; nor, has any other jurisdiction construed or applied Ohio law in reaching its determination. While I do not assert that decisions from other jurisdictions are controlling in Ohio, I cannot accept the majority's summary disposition of these foreign decisions. First, this court, in the past, has recognized the persuasive value of decisions from other jurisdictions in this area. See *Ohio Water Service Co.* v. *Pub. Util. Comm.* (1980), 64 Ohio St. 2nd 12. Second, the

near unanimity of decisions from other jurisdictions allowing amortization of these types of expenditures further demonstrates the reasonableness of the commission's decision in this case.

Appellants urged before this court that before any expense or cost could be passed on to the ratepayers, it must confer a direct and primary benefit upon said ratepayers. Implicit in the majority's decision is an acceptance of this argument. Thus, the majority, today, takes another step toward entrenching the spurious "direct, primary benefit" test into the public utilities law of Ohio.[9]

"Review of orders of the Public Utilities Commission on appeal is limited to a consideration of whether the order is unreasonable or unlawful***." *Cremean v. Pub. Util. Comm.* (1976), 48 Ohio St. 2d 163, paragraph one of the syllabus. The order in the instant cause is neither unreasonable nor unlawful. Accordingly, I would affirm the decision of the commission in its entirety.

HOLMES, J., concurs in the foregoing concurring and dissenting opinion.

LOCHER, J., concurring in part and dissenting in part. I concur in the syllabus and Parts III (notice and staff investigation) and IV (amortization) of the majority opinion. I would also note, however, that the financial effect of this decision on CEI will be insignificant. CEI informed its investors in its "1979 Annual Report":"*** The Company [CEI] will seek the approval of the Federal Energy Regulatory Commission and The Public Utilities Commission of Ohio for authority to amortize [the costs previously expended toward the four nuclear units whose construction CAPCO terminated] over a suitable number of years. The extent to which these costs may be recovered

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[9] See Justice Herbert's dissent in *Cleveland* v. *Pub. Util. Comm.* (1980), 63 Ohio St. 2d 62, 75, in which I concurred.

through rates will be determined by the PUCO. If any costs of termination are not permitted to be recovered, the Company would be required to reduce Net Income by the disallowed amount. In any event, the resolution of these matters should not have a material adverse impact on the financial position of the Company."

I dissent from Part I of the majority opinion (CWIP), because PUCO refuses to define standards for review of CWIP matters. My dissenting opinions in *Consumers' Counsel* v. *Pub. Util. Comm.* (1979), 58 Ohio St. 2d 108, 117, and *Consumers' Counsel* v. *Pub. Util. Comm.* (1981), 66 Ohio St. 2d 162, 167, express the reasons for my concern.

APPENDIX D

Decision and Opinion of the Public Utilities Commission of Ohio

(Filed July 10, 1980)

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of The Cleveland Electric Illuminating Company for Authority to Amend and Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service.	Case No. 79-537-EL-AIR
In the Matter of the Complaint and Appeal of The Cleveland Electric Illuminating Company from Ordinance No. 1673-79 of the Council of the City of Cleveland, Ohio Passed August 7, 1979, entitled "An Ordinance Setting the Maximum Rates which may be Charged by The Cleveland Electric Illuminating Company for Electric Service Within the City of Cleveland".	Case No. 79-774-EL-CMR

OPINION AND ORDER

The Commission, coming now to consider the above-entitled permanent rate application filed by the Cleveland Electric Illuminating Company pursuant to Section 4909.18 Revised Code and the above-styled complaint and appeal filed by the Cleveland Electric Illuminating Company pur-

suant to Section 4909.34 Revised Code; the Staff Report of Investigation issued pursuant to Section 4909.19 Revised Code; having appointed its attorney examiner, Barth E. Royer, pursuant to Section 4901.18 Revised Code to conduct a public hearing and to certify the record thereof directly to the Commission; the testimony and exhibits introduced into evidence at the public hearing commencing April 2, 1980, and concluding May 22, 1980; its prior Entries and Orders in these dockets; and being otherwise fully advised in the premises and in compliance with Section 4903.09 Revised Code, hereby issues its Opinion and Order.

History of the Proceedings:

The Cleveland Electric Illuminating Company, the applicant herein, is an Ohio corporation engaged in the business of supplying electric service in this state. The company provides retail service to some 699,000 customers in a 1,700 square mile service territory which encompasses the greater Cleveland area as well as all or parts of nine northeastern Ohio counties. As a public utility and an electric light company within the definitions of Sections 4905.02 and 4905.03(A)(4) Revised Code, applicant is subject to the jurisdiction of this Commission pursuant to Sections 4905.04, 4905.05, and 4905.06 Revised Code. The company's present rates for electric service were established by the May 2, 1979 Opinion and Order of this Commission in Case No. 78-677-EL-AIR, as subsequently modified by the Order on Rehearing in that docket of March 5, 1980.

On June 19, 1979, the Cleveland Electric Illuminating Company served and filed a notice of its intent to submit a permanent rate increase application pursuant to Section 4909.18 Revised Code as required by Section 4909.43(B) Revised Code and Rule 4901-1-36 Ohio Administrative Code. As a part of this prefiling notification, applicant re-

quested that June 30, 1979, be fixed as the date certain for the valuation of property and that the twelve months ending December 31, 1979 be established as the test period for the analysis of accounts. The Commission approved the proposed date certain and test year by Entry of July 5, 1979. By motion of August 3, 1979, applicant requested a waiver of certain of the Commission's Standard Filing Requirements. This motion was granted in part and denied in part by Commission Entry of August 22, 1979. The application itself was filed September 17, 1979. The Commission accepted the application for filing by Entry of October 19, 1979, and approved the proposed form of the required legal notice subject to certain modifications.

On August 7, 1979, the Council of the City of Cleveland passed Ordinance No. 1673-79, which continued in effect the Illuminating Company's existing rates for service within that municipality for a two-year period commencing June 19, 1980. The company filed a complaint and appeal from said ordinance pursuant to the provisions of Section 4909.34 Revised Code on August 31, 1979. By Entry of September 26, 1979, the Commission determined that the evaluation of the complaint and appeal should be conducted with reference to the same date certain and test year previously approved in connection with the pending general rate application and that the two cases should be consolidated. The company submitted the information required by the Standard Filing Requirements on November 19, 1979, and the Commission, by Entry of December 12, 1979, accepted the complaint and appeal for filing as of that date. An amended proposed form of legal notice was approved for publication.

By its Entry of August 8, 1979, in Case No. 79-525-EL-ATA, the Commission approved the application of the Cleveland Electric Illuminating Company for authority to establish rates and terms and conditions of service for electric street lighting service. Proposed tariff sheets gov-

erning this service were accepted for filing pursuant to Section 4909.18 Revised Code as an application not for an increase in rates. However, in its Entry of October 5, 1979, issued in response to rehearing applications filed by certain affected municipalities, the Commission concluded that a rehearing should be granted for the purpose of reviewing the reasonableness of the new street lighting tariffs. The Commission directed that this matter be consolidated for hearing with the pending rate case.

In accordance with the provisions of Section 4909.19 Revised Code, the Staff of the Commission conducted an investigation of the matters set forth in the application and the complaint and appeal. A written report of the results of the staff investigation was filed March 4, 1980, and was served as provided by law. Objections to the Staff Report were timely filed by the applicant and by the following intervenors: the Office of Consumers' Counsel; the City of Cleveland, Senior Citizens, *et. al.;* Industrial Electricity Consumers; and the City of University Heights.

Pursuant to the Commission's Entry of March 12, 1980, the public hearing of these matters commenced April 2, 1980, before attorney examiner Barth E. Royer. The first day of hearing was held at City Hall in Cleveland, Ohio, to afford members of the public affected by these cases the opportunity to present statements concerning the proposed increase. Subsequent sessions were held at the offices of the Commission, 180 East Broad Street, Columbus, Ohio. The recorded transcript of the proceeding and the exhibits admitted into evidence during the 32 days of hearing have now been certified to the Commission by the examiner for its consideration.

Appearances:

Mr. Alan D. Wright, General Counsel, and Mr. Craig I. Smith, Senior Counsel, 55 Public Square, Cleveland, Ohio; and Messrs. Squire, Sanders & Dempsey, by Messrs.

Alan P. Buchmann, Lowell L. Garret, William C. Donahue, and Richard W. McLaren, Jr., 1800 Union Commerce Building, Cleveland, Ohio; on behalf of the applicant, the Cleveland Electric Illuminating Company.

Mr. William J. Brown, Attorney General of Ohio, by Messrs. Thomas L. Mumaw, David Neubauer, and James Bacha and Ms. Judith B. Sanders, Assistant Attorneys General, 180 East Broad Street, Columbus, Ohio, on behalf of the Staff of the Public Utilities Commission of Ohio.

Mr. James E. Wagner, Director of Law, and Mr. James L. Harkins, Jr., Assistant Director of Law, Cleveland City Hall, 601 Lakeside Avenue, Cleveland, Ohio; and Mr. Henry W. Eckhart, 88 East Broad Street, Columbus, Ohio; on behalf of the City of Cleveland, Ohio.

Mr. William A. Spratley, Consumers' Counsel, by Mr. Gary M. Petroff and Ms. Gretchen J. Hummel, Associate Consumers' Counsel, 137 East State Street, Columbus, Ohio, on behalf of the Office of Consumers' Counsel.

Mr. Joseph P. Meissner, Cleveland Legal Aid Society, 1223 West 6th Street, Cleveland, Ohio, on behalf of the Senior Citizens Coalition, the Cleveland Welfare Rights Organization, Inc., the Western Reserve Alliance, the Cleveland Chapter of Ohioans for Utility Reform, and North Shore Alert, intervenors.

Messrs. Bell & Clevenger, L.P.A., by Messrs. Langdon D. Bell, and Samuel C. Randazzo, 21 East State Street, Columbus, Ohio, on behalf of Industrial Electricity Consumers (Aluminum Corporation of America, Chase Brass and Copper Company, Inc., General Motors Corporation, Jones and Laughlin Steel Corporation, Olin Corporation, and Union Carbide Corporation), intervenors.

Mr. Guerin L. Avery, Law Director, Brainard Place-Suite 333, 29001 Cedar Road, Lyndhurst, Ohio, on behalf of the City of University Heights, Ohio, intervenor.

Commission Review and Discussion:

These cases come before the Commission upon the application of the Cleveland Electric Illuminating Company pursuant to Section 4909.18 Revised Code for authority to increase its rates and charges for electric service to its jurisdictional customers and upon the company's complaint and appeal pursuant to Section 4909.34 Revised Code from Ordinance No. 1673-79 of the City of Cleveland, Ohio, whereby it is charged that said ordinance, which would continue applicant's present rates in effect, is unreasonable and unlawful. Applicant alleges that its existing rates are insufficient to provide it reasonable compensation for the service it renders customers affected by these proceedings and seeks Commission approval of rate schedules which would yield some $79,795,000 in additional gross annual revenues based on its analysis of test-year operations. This additional revenue represents an increase of approximately 10.3 percent over that currently realized from service to jurisdictional customers. It now falls to the Commission to evaluate the evidence of record in order to determine if applicant's existing jurisdictional rates are inadequate and if the ordinance appealed from is unreasonable. In the event applicant is found to have sustained its burden of proof with respect to these matters, the Commission must then establish rates which will afford the company the opportunity to earn a fair rate of return.

Also before the Commission for consideration at this time is Case No. 79-525-EL-ATA, an application by Cleveland Electric Illuminating Company to establish rates and terms and conditions of service for providing electric street lighting within its service territory. Although the Commission has previously accepted this tariff as an application not for an increase in rates by its entry in this docket of August 8, 1979, specific provision was made in

its rehearing entry of October 5, 1979, for a review of the reasonableness of the rates contained therein in the context of the pending rate proceedings. We will address the street lighting matter through a separate opinion.

JURISDICTIONAL ALLOCATIONS

In assigning rate base and demand-related expenses to the customers affected by the instant application and complaint and appeal, the applicant generally followed the two-peak allocation methodology accepted by the Commission in its prior case (App. Ex. 6B, p. 8). However, in developing the allocation factors to be used for purposes of these proceedings, the company used a projected summer and winter peak rather than relying on historical data for determining weighted seasonal peak demands. Further, applicant also adjusted the power plant capacity ratios to reflect an anticipated decline in nonjurisdictional load levels resulting from a reduction in contract demand associated with service to the Cleveland Department of Public Utilities (App. Ex. 6B, pp. 2-3). The staff recommends that these allocation procedures be rejected and proposes, in lieu thereof, a 12-month coincident peak method for determining demand allocation (S. R., pp. 3-6). Applicant has objected to the staff recommendation.

As the Commission has observed on prior occasions, there are a number of valid allocation techniques available; but the choice in a given case must turn on which of the methods proposed most accurately recognizes power cost causation in light of the operating characteristics of the utility in question (*Ohio Power Company*, Case No. 75-161-EL-SLF [August 4, 1976]). It should be apparent that the two-peak method is only appropriate for those companies which exhibit a pronounced summer and winter peak. Although applicant may have fit this description

in the past, the test-year data, as the staff points out, shows a leveling of the monthly peaks (S.R., pp. 4-5, Tr. XX, p. 117). The lowest actual 1979 monthly peak (October) was 87 percent of the highest monthly peak (July) (S.R., pp. 4-5). In six other months, the peak was in excess of 95 percent of the annual peak (App. Ex. 6C). When the 1979 monthly peaks are plotted graphically, it is evident that the peaks have become hills and that the valleys have filled in (Tr. XX, p. 117). If the Commission limits its analysis to this data, it is clear that the staff's 12-month coincident peak method should be preferred. Indeed, this is the method applicant uses before the Federal Energy Regulatory Commission, although, in fairness, it should be noted that the FERC apparently now requires the use of the 12-month method (S.R., p. 5, Tr. XV, p. 13).

Applicant attempts to justify its continued use of the two-peak method by relying on estimates of the 1980 summer and winter peaks which, it contends, more accurately portray expected conditions. This novel approach is attended by several significant problems. First, from a conceptual standpoint, there should be some matching of the data sets involved in the determination of the allocation ratios and the property and expenses to which they are to be applied. After all, the purpose of the exercise is to assign existing plant based on existing demand, not to allocate future plant constructed to serve some future level of demand. However, quite apart from this theoretical consideration, is the question of the reliability of applicant's projections. The company attacks the staff method by claiming it does not adequately consider normal weather conditions (Tr. XX, pp. 113-115), an assumption automatically taken into account in applicant's forecast. No one disputes that temperature is a significant factor, but there are also other factors to be assessed such as the level of economic activity in the service territory, the

availability of the natural gas heating alternative, the impact of conservation efforts, the effect of rapidly increasing electric rates, and the track record of the company in predicting peak loads. On balance, the Commission does not believe that the test year data relied on by the staff is so unrepresentative as to yield an unreasonable result. Finally, we come to applicant's complaint that the staff method does not adequately consider daily operating characteristics because ten of the twelve monthly peaks were daytime peaks (App. Brief, pp. 27-28). Applicant attaches great significance to figures indicating that its daily load exceeds 90 percent of the daily peak for fifteen to nineteen hours on an average weekday basis (Tr. XV, p. 14). Because its projected winter peak is an evening peak, applicant contends that its method more properly weights the evening load's contribution to capacity requirements. This argument loses sight of the fact that both methods are peak responsibility methods and have nothing whatever to do with load duration. If applicant believes this diversity factor to be of such critical importance, the company should employ an allocation method specifically designed to recognize it rather than risk using a method which, in theory, could have resulted in the selection of two daytime peaks, thereby losing the evening load's contribution in its entirety. In fact, had applicant used calendar 1979 data, this would have been the case (App. Ex. 6C). The Commission does not believe that the staff method, which at least affords twelve measurements instead of only two, can be faulted on this score.

In light of the foregoing discussion, the Commission is of the opinion that the staff's 12-month method should be adopted for purposes of these proceedings. Although we do not view the fact that the FERC mandates the use of this method as being in any way controlling for the purposes at hand, there is a certain comfort in the sym-

metry resulting from using the same allocation method in both jurisdictions; the sum of the parts cannot be greater than the whole. Further, the Commission finds applicant's proposed adjustment to reflect the anticipated reduction in contract demand associated nonjurisdictional service to the Cleveland Department of Public Utilities to be inconsistent with the matching concept referred to above. Although the Commission would agree that this change will have some impact on the nonjurisdictional load, we cannot conclude that this will be the only factor affecting the jurisdictional-nonjurisdictional load mix during the period these rates will be in effect. Moreover, this minor change in the contract demand does not automatically mean that the actual demand will track the reduction precisely. The evidence indicates that during the test year, when the Cleveland Department of Public Utilities contract called for 80 megawatts, monthly peaks actually ranged from 69.4 to 90.0 megawatts (Staff Ex. 2, pp. 6-7). The possible effect of this single change is not enough to convince the Commission to shelve the test-year concept. We, therefore, accept as reasonable the allocation ratios proposed by the staff.

RATE BASE

The applicant, the Commission staff, and Consumers' Counsel each offered testimony and submitted exhibits in support of their respective rate base proposals in these proceedings. The following table compares the company and staff estimates of the value of applicant's property used and useful in rendering the service affected by the application and the complaint and appeal as of the date certain of June 30, 1979. The adjustments to these proposals recommended by the various intervenors will be discussed on an item-by-item basis below.

Jurisdictional Rate Base

(000's Omitted)

	Applicant[1]	Staff[2]
Plant In Service	$1,889,583	$1,876,927
Depreciation Reserve	(464,602)	(466,049)
Net Plant In Service	$1,424,981	$1,410,878
CWIP	95,501	91,521
Working Capital	128,394	62,035
Deferred Taxes and Tax Credits	(25,687)	(79,215)
Jurisdictional Rate Base	$1,623,189	$1,486,049

[1]App. Rev. Sched. B-1

[2]Staff Ex. 7, Appendix D, Rev. Sched. 7.1

The difference between the respective plant in service determinations of the applicant and the staff is, in part, attributable to the difference in the allocation methodologies employed. There are, however, additional reasons for the discrepancy in these figures which must be explored, as well as other related issues arising from intervenors' objections which must be considered.

Land and Land Rights:

As a part of its investigation in these proceedings, the Commission staff reviewed the company's land accounts in order to assure that the real property proposed for inclusion in rate base satisfied the statutory used and useful requirement. Similar staff analyses in prior cases involving this company have resulted in some transfers to future use or non-utility property accounts, and the staff inspection of additional parcels in connection with the cases now before us has again produced a recommendation that the rate base be adjusted (S.R., pp. 21-22). Specifically, the staff concluded that a deduction in the amount of $368,938 was appropriate based on its finding that three ash disposal

sites associated with the East Lake plant were no longer used and useful and its opinion that the acreage at the Inland substation and Strongsville service center was in excess of that reasonably required for utility operations (S.R., p. 21; S.R., Sched. 8.2; Staff Ex. 2, pp. 8-11). Applicant objected to the deduction from rate base of the original cost dollars represented by these parcels and, through its witness Kemper, presented evidence in support of its position that the property in question was used and useful at date certain (App. Ex. 3A, pp. 4-7).

The staff excluded the Vine, Syracuse A, and Syracuse B ash disposal sites based on its conclusion that the capacity of these areas to receive fly ash had been exhausted. Applicant points out that one of the sites can still accommodate fly ash and is also being used to store cinders which are eventually sold to municipalities (App. Ex. 3A, p. 4). The Commission agrees that the value of this parcel, $25,499, must be restored to rate base. The Commission does not agree, however, that the other two ash disposal sites constitute used and useful property as contemplated by the statute. Applicant acknowledges that these two parcels are filled to capacity, but argues that they are still satisfying one of their original purposes, holding fly ash. Further, the company claims that the sites have little resale value and, because land is not depreciable property, there is no way that any cost recovery or return can be realized unless the parcels are included in rate base. There is no merit in either of these arguments. Property can only be considered used and useful if it is utilized in providing service. The record is clear that the two parcels in question can no longer receive fly ash; thus, they do not meet this requirement. Moreover, the fact that the parcels may have limited resale value is totally irrelevant. Once the property has been found not to be used and useful, it goes without saying that ratepayers cannot be required to contribute toward a return on it. The Commission, therefore, accepts

the staff's rate base adjustment for these two ash disposal sites.

The staff's proposed deductions for excess land at the Inland substation and the Strongsville service center present much closer questions (Staff Ex. 2, pp. 10-11). The Commission has previously recognized that there are a number of factors which must be considered in evaluating adjustments involving the elimination of minor portions of land parcels on the theory that the total acreage at a site is above that reasonably required to support a given installation (*Ohio Edison Company,* Case No. 78-1567-EL-AIR, *et al.* [January 30, 1980]). Obvious practical constraints exist upon obtaining precisely the acreage necessary for a particular operation, and there is a possibility that severance damages would actually produce a net detriment to the ratepayer if a somewhat smaller parcel had, in fact, been acquired. Although the site maps introduced by the applicant might appear to suggest the need for this type of analysis in this case (App. Ex. 3A, pp. 28-29), the Commission finds the critical evidence in this area to be the admissions of applicant's own witness with respect to the company's specified plans for the future use of much of the area excluded by the staff at these two locations (App. Ex. 3A, pp. 5-6). Given this state of the record, we conclude that the dollar associated with these areas should properly be assigned to Account 105 (Land Held for Future Use) until such time as the planned construction is accomplished. Applicant's objection to the staff adjustments should be overruled.

Beaver Valley Common Facilities:

In arriving at its recommended rate base for purposes of these proceedings, the Commission staff excluded from plant in service the amount of $8,894,241 which represents applicant's share of the common facilities at the Beaver Valley nuclear generating plant (S.R., p. 22; S.R.,

Sched. 8.1). Because applicant's ownership interest in Beaver Valley is limited to Unit No. 2, a unit still under construction, the staff concluded that it would be improper to consider the company's share of the common facilities, although completed in connection with the first Beaver Valley unit, as used and useful property until such time as Unit No. 2 is placed in service. Applicant objects to the staff's treatment.

The Commission has had occasion to consider this precise question in a number of its recent decisions, including that issued in this company's last rate case (*Cleveland Electric Illuminating Company,* Case No. 78-677-EL-AIR [May 2, 1979]; *Ohio Edison Company,* Case No. 77-1249-EL-AIR [November 17, 1978]; *Toledo Edison Company,* Case No. 79-143-EL-AIR [February 29, 1980]). We have repeatedly held the staff adjustment to be proper, and nothing presented in this record would persuade us to alter that view (App. Ex. 4, pp. 43-44). Although the Commission recognizes that FERC accounting principles require that common facilities be classified as plant in service at the time the first unit is placed in service, this does not change the fact that the common facilities in question do not satisfy the statutory criteria for rate base eligibility (Section 4905.15(A)(1) Revised Code). Cleveland Electric Illuminating Company does not own Beaver Valley Unit No. 1. Although applicant's customers may, from time to time, receive power from the first Beaver Valley unit by virtue of certain CAPCO transactions, this does not render the portion of the common facilities assignable to Unit No. 2 used and useful property for ratemaking purposes. This objection is again overruled.

Applicant contends that if the common facilities are to be eliminated from rate base, consistency requires that the Commission direct the company to reclassify this property as plant held for future use, to cease accruing depreciation, and to resume the accumulation of AFUDC until

such time as Unit No. 2 is transferred to plant in service (App. Ex. 4A, p. 49). The staff has also recommended a reclassification of the property (S.R., p. 22). In the *Toledo Edison* case, *supra,* the Commission agreed that the principles underlying the exclusion of the common facilities from rate base dictate that the property be reclassified for Ohio regulatory purposes and directed that depreciation accruals be stopped. The Commission did not reach the question of the resumption of AFUDC in the context of that decision, but believes that such a measure would be inconsistent with the classification of the property as plant held for future use. The Commission, therefore, orders applicant to reclassify the Beaver Valley common facilities and to cease accruing depreciation. Applicant's proposal to resume AFUDC must be rejected.

Davis-Besse Nuclear Plant:

Through their filed objections, intervenors City of Cleveland and Senior Citizens *et al.,* contend that applicant's share of the Davis-Besse nuclear plant, a generating facility co-owned by Cleveland Electric Illuminating Company and Toledo Edison Company, should be excluded from the rate base on the theory that the plant is not "used and useful" within the meaning of that term as employed in Section 4909.15(A)(1) Revised Code. The Commission is on familiar ground in considering these objections as the City of Cleveland advanced similar arguments in the company's last rate proceeding (*Cleveland Electric Illuminating Company,* Case No. 78-677-EL-AIR [May 2, 1979]). The Commission's finding in that case that Davis-Besse was properly includable in rate base has just been affirmed by the Supreme Court (*City of Cleveland v. Public Utilities Commission,* S.Ct. Case No. 79-1158 [July 9, 1980], 63 Ohio St. 2d [1980]). Although a considerable portion of the record now before us is devoted

to this question, when the law and the evidence are sifted out from the rhetoric and the statements of counsel, the Commission once again comes to the same inescapable conclusion. Davis-Besse must and should be included in the rate base. This is a most difficult issue to address, not because it presents a close question, but because much of intervenors' attack is so illogical as to defy analysis (See, Tr. XXIII, pp. 73-81).

Rather than begin with counsel for the City of Cleveland's repeated charge that Davis-Besse is a "white elephant" that is unsafe and unreliable (City of Cleveland Brief, p. 4), it may prove more fruitful to begin with an unimpassioned look at the facts. No one, including company witnesses who were examined on the subject, disputes the fact that the unit's 1979 performance was extremely disappointing (Tr. VIII, p. 67). The plant actually produced only some 59 percent of its budgeted generation during the test year (Senior Citizens Ex. 1). It exhibited a unit capacity factor in 1979 of only 39.4 percent (City of Cleveland Ex. 2L). Davis-Besse was forced off line 15 times during the test period, although in five of those instances the duration of the outage was less than one day (City of Cleveland Ex. 8). The principal reason for the unit's poor annual availability factor was the 103-day shutdown mandated by the Nuclear Regulatory Commission in the wake of the Three Mile Island incident (City of Cleveland Ex. 8). In terms of production expense, Davis-Besse is by far the cheapest source of energy available to the company (City of Cleveland Ex. 4). Despite the three month outage referred to above and another extended outage in December of 1979, the unit contributed over 1.6 billion Kwh to applicant's system generation during the test year, roughly 10 percent of the company's total production (City of Cleveland Ex. 4). Where, in these facts, is there support for the proposition that Davis-Besse is not used and useful?

Senior Citizens, *et al.*, suggests that if the plant cannot be excluded from rate base in its entirety, then, at minimum, the Commission should eliminate a portion of its value based on a calculation comparing its actual performance to its expected performance. The contention that utility property may be considered partially used and useful for rate base purposes is akin to the suggestion that someone can be partially pregnant. There is a well-established regulatory technique for dealing with the situation in which a generating unit exhibits an unusually high forced outage rate during the test year. The proper response is not the exclusion of all or part of the plant from rate base, but rather a normalizing adjustment to test period operations which excludes the costs associated with the outages in the calculation of future rates. This is precisely what the applicant and the staff have proposed in this case (App. Ex. 1, Sched. 3.12; S.R., p. 12). The approval of such an adjustment for ratemaking purposes places the ratepayers in exactly the same position with respect to future rates as if the plant had operated at anticipated levels.

At this point, intervenors' arguments became more difficult to comprehend. The Commission assumes they understand that operations have been normalized, so they must be suggesting that even if the plant performed as expected, it should still be excluded from rate base. Intervenors assert that the plant is unsafe and suffers from significant design and construction defects. The Commission is, of course, concerned about the risks associated with nuclear generation in general, and Davis-Besse in particular; but this is an area where the federal government has clearly pre-empted state regulatory authority. *Northern States Power Co. v. Minnesota*, 447 F.2d 1143 (8th Cir., 1971), *aff'd*, 405 U.S. 1035 (1972). *See also, Stebbins v. Public Utilities Commission*, S.Ct. Case No. 79-1622 (June 25, 1980), 62 Ohio St. 2d(1980). Moreover, nothing in this record indicates that the plant is unsafe.

What the evidence does show is that in each instance where a problem forced the unit off line, the problem was identified, reported, and remedied to the satisfaction of the Nuclear Regulatory Commission, the agency that does have authority in this area. It is true that the NRC has ordered a number of modifications, and that some of these have been quite costly (Tr. XXIII, p. 130); but it must be remembered that the plant has been subject to NRC scrutiny since the time it was on the drawing board and that it was and is licensed to operate.

Subsequent to the Commission order in the company's last case, the Supreme Court of Ohio issued its decision in *Consumers' Counsel v. Public Utilities Commission,* 58 Ohio St.2d 449 (1979). This case represented an appeal of a Toledo Edison rate order (*Toledo Edison Company,* Case No. 76-1176-EL-AIR [June 9, 1979]) wherein the Commission had determined that the Davis-Besse plant should be considered used and useful and, therefore, includable in rate base despite the fact that it had not been assigned commercial operating status before the date certain. The Commission based this conclusion on the fact that the unit had been synchronized with the system and was producing electricity, albeit through test generation, prior to date certain. The Court reversed, finding as follows:

> "It would be inequitable to prematurely shift the risk of plant failure from the utility's investors to the ratepayers by the inclusion in the rate base of highly complex and innovative technology which has not been proven to be reasonably free from significant design or construction defects. The initial risk of failure is appropriately borne by the investors, who have undertaken the project and who will ultimately profit from its success. It is only proper that their venture be found operational before they commence to recoup their capital outlays from the consumers." *Consumers' Counsel, supra,* pp. 456-457.

Intervenors, consistent with their assertion that the plant is unsafe, place great emphasis upon this language

as support for the proposition that Davis-Besse should not be included in the rate base in this case. However, the fact pattern presented to the Court in *Consumers' Counsel, supra,* was quite different than that with which the Commission is confronted in the instant proceedings. In that case, although there was test generation, the unit was not producing net energy for the consumer before the date certain. Here, the plant in question has been operational since 1977; the date certain was June 30, 1979. It has produced vast quantities of energy during that period of time. This is not a date certain timing problem of the type addressed by the Court. Further, if the Commission were to deny the company a return on Davis-Besse, consistency would require that test-period operations be adjusted to reflect an assumption that the plant was not available. We doubt that consumers would appreciate the impact of such a measure.

The City of Cleveland accuses the Commission of failing to recognize that applicant's share of Davis-Besse ended up costing about four times more than the company originally expected (Tr. VIII, p. 74) and that if these costs, plus the costs still being incurred to meet changing NRC requirements, are taken into account in computing costs per Kwh, Davis-Besse is no bargain. Intervenor goes so far as to assert that "the capital costs associated with Davis-Besse are the primary cause of the CEI financial problems" (City of Cleveland Brief, p. 4). Assuming for the sake of argument that this statement is correct, how would the exclusion of the plant from rate base do anything but exacerbate these problems? The fact is that the capital costs associated with the construction of all types of capacity have skyrocketed (Tr. VIII, p. 61). Although the problem is more acute with respect to nuclear plants due to ever-tightening licensing requirements, the hope was and is that the output from Davis-Besse over its life will cost substantially less than any alternative construction the company could have undertaken in the same time frame

(Tr. VIII, p. 69). The relevant point is that the investment in the plant has been made, the plant is providing service, and the suppliers of the required capital are entitled to a return on their investment.

There are other inconsistencies in intervenors' arguments that should not go unnoticed. The City of Cleveland complains that it costs the ratepayers approximately $800,000 per week for each week the plant does not operate (City of Cleveland Brief, p. 3). Which way does this cut? We would have thought that this testifies to the benefit of having Davis-Besse on the system. Then, there is the suggestion by Senior Citizens, *et al.*, that the uncertainties associated with Davis-Besse increase risk, thereby driving up investors' return requirements (Senior Citizens Brief, p. 21). We would merely inquire as to what impact on the company's cost of capital intervenor would anticipate were the Commission to disallow any return on the tremendous investment in this plant as it would have us do. Finally, we come to the theory that if the Commission includes Davis-Besse in rate base, the company will have no incentive to seek legal redress for any losses occasioned by the alleged defects in the design or construction of the unit or by the alleged negligence of Toledo Edison personnel in managing its operation. Senior Citizens'. *et al.*, even suggests that if the Commission recognizes Davis-Besse for ratemaking purposes, such a step would afford a defense in any legal action that applicant might maintain. These arguments are totally without merit. In the first place, they assume that the company has some actionable claim arising out of the unit's admittedly poor performance. It would certainly be improper for the Commission to engage in speculation in this area, and even more improper to base a rate case deduction on the innuendo of intervenors' attorneys. Detailed contracts and agreements govern applicant's relationship with those firms that constructed and operate Davis-Besse. Intervenors should examine their provisions before spread-

ing these assertions on the record. The Commission cannot deny applicant a return on this plant at this point in time with the instruction that it go sue someone or other in hopes that it will recover something from them in the future. If it should eventuate that applicant does obtain some recovery through litigation, whether involving Davis-Besse or any other aspect of its operation, under circumstances where customers are entitled to share in the benefits the Commission will see to it that they are properly credited (*Ohio Power Company*, Case No. 77-380-EL-FAC (February 7, 1979); *Ohio Power Company*, Case No. 78-676-EL-AIR [April 16, 1979]). There is simply no basis in law or fact for excluding all or part of the net original cost of Davis-Besse from the rate base determined for purposes of these proceedings.

Excess Capacity:

The Commission staff, as a part of its investigation in these proceedings, examined applicant's generating capacity to determine whether capacity exists which exceeds that reasonably required to meet the company's net peak demand and afford a reasonable reserve margin. As a result of this review, the staff concluded that applicant's production system was not excessive (S.R., pp. 22-23; Tr. XXI, pp. 114-120). Intervenors City of Cleveland and Senior Citizens, *et al.*, object to the staff's finding, contending that the staff analysis was inadequate and that the company does have excess capacity. Claiming, without a shred of evidence as to why the figure should be accepted, that a 20 percent reserve margin is appropriate, intervenors propose a rate base deduction, never quantified, to exclude capacity in excess of this amount on the theory that such property is not used and useful. The short answer here would be to simply point out that there is nothing in this record, save for intervenors' bare assertions, that would support these objections. However, the Commission will

once again set out the considerations which must be taken into account in dealing with this question.

This so-called "excess capacity" issue has been before the Commission time and time again in recent years in cases involving almost all major electric companies subject to our jurisdiction, including this applicant. (See *e.g., Dayton Power and Light Company,* Case No. 76-823-EL-AIR [July 22, 1977]; *Monongahela Power Company,* Case No. 76-824-EL-AIR [September 7, 1977]; *Dayton Power and Light Company,* Case No. 78-92-EL-AIR [March 9, 1979]; and *Cleveland Electric Illuminating Company,* Case No. 78-677-EL-AIR [May 2, 1979]). One fact that has clearly emerged from these cases, as it has from the record in the instant proceedings, is that it is most inappropriate to measure the reasonableness of existing capacity levels by a simple comparison to some assumed ideal reserve margin (Tr. VIII, pp. 106-109; Tr. XXI, pp. 116-117). Reserve requirements are company-specific, and what is reasonable for one electric utility may not be reasonable for another depending on factors such as unit sizes and generation mix. Next, assuming appropriate reserve criteria can be established, it must be recognized that in light of the extensive lead times involved in the construction of generating facilities and the variety of factors which can influence load growth, it is obviously unrealistic to assume that any utility would have the forecasting capability which would allow it to add capacity in the precise increments required to maintain the theoretically appropriate margin. This problem is intensified by the large size of the units being added today. Thus, the relevant inquiry is not whether the reserve at any point in time matches some optimum margin, but whether, given all those factors which can influence construction and load growth, the company can be fairly said to have acted imprudently in its capacity planning. As we will discuss in more detail *infra,* there has been no showing that this has been the case with respect to this applicant.

Finally, there is the conceptual problem which attends a capacity adjustment based on the theory that a portion of a company's production capacity is not used and useful. All applicant's generating stations, although they may have been downrated or off line from time to time, were in service meeting customer demand pursuant to principles of economic dispatch during the test period. Thus, each unit, standing alone, clearly would meet the used and useful requirement. A percentage adjustment to system capacity ignores the reality that such capacity is comprised of individual units which represent actual substantial dollar investments committed to assure that adequate service can be maintained. As the Commission stated in the *Columbus and Southern* decision cited above:

> "Hindsight is always perfect, and before the Commission will consider denying a return on property actually used in providing service something more need be shown than that the company's foresight was not."

Intervenors' objections are, hereby, overruled.

Depreciation Reserve:

Section 4909.05(H) Revised Code requires that the Commission determine the proper and adequate reserve for depreciation to be deducted from the original cost of applicant's used and useful property. The staff, in the course of its investigation, tested applicant's booked reserve against a theoretical reserve study based on date certain balances and found excellent correlation, indicating that the booked reserve might properly be relied on for ratemaking purposes (S.R., pp. 23-24). The staff did take exception, however, to a retroactive adjustment to the reserve performed by applicant in order to reflect the change to the units-of-production method of depreciation for the nuclear plant accounts as authorized by this Com-

mission in *Determination of Depreciation Charges,* Case No. 77-1369-EL-UNC (December 12, 1979). The Commission considered this same question in its order in *Toledo Edison Company,* Case No. 79-143-EL-AIR (February 29, 1980), finding such an adjustment to be appropriate. The staff revised its recommendation at hearing to conform to that decision and this step, together with a correction to reflect normalized generation for Davis-Besse, essentially removes the matter from controversy (Staff Ex. 2, pp. 11-12). The remaining differences between the applicant and staff reserve recommendations are tied to their respective positions on certain other rate base, allocation, and normalization issues. As those questions have been resolved in favor of the staff, the Commission adopts the staff's proposed jurisdictional depreciation reserve of $466,049,256 as the proper deduction from plant in service for purposes of these proceedings (Staff Ex. 3, Rev. Sched. 9). Deducting this amount from the original cost of includable property results in a finding of jurisdictional net plant in service of $1,410,903,292.

Construction Work In Progress:

Section 4909.15(A)(1) Revised Code provides that the Commission, in its discretion, may include in its rate base determination a reasonable allowance for construction work in progress. The statute limits eligibility for the allowance to projects which are 75 percent complete, and there is a further prohibition against authorization of such an allowance to the extent it would exceed 20 percent of the total valuation not including this item (Section 4909.15 (E) Revised Code). For purposes of these proceedings, applicant originally requested an allowance for construction work in progress of $99,263,076, which reflected the jurisdictional date certain costs associated with some 171 job orders considered by the company to represent qualifying projects (App. Ex. 1, Sched. B-4). The requested

allowance was subsequently reduced to $95,501,269 in light of applicant's acceptance of a staff adjustment which reclassified 48 of the job orders based on a finding that the construction in question was complete and the property in service at date certain (App. Ex. 3A, p. 28; App. Rev. Sched. B-1). The staff recommends a jurisdictional allowance of $91,521,464 (S.R., pp. 24-25; S.R., Sched. 10). Consumers' Counsel, although opposed in principle to an allowance for construction work in progress, has accepted the staff's recommendation as reasonable (O.C.C. Ex. 1, pp. 7-8); but the City of Cleveland and Senior Citizens, *et al.*, contend that there should be no construction work in progress allowance authorized in these cases.

The claims of the intervenors opposing any allowance for construction work in progress require no more than a cursory discussion, as much of what has been argued here has been heard and rejected many times in the past (See *Ohio Edison Company,* Case No. 78-1567-EL-AIR [January 30, 1980] and cases summarized therein). Senior Citizens' contention that the statute creating the allowance is unconstitutional has been definitively laid to rest (*Consumers' Counsel v. Public Utilities Commission,* 58 Ohio St. 2d 108 [1979]), and its charge that the Commission is "stumbling along" trying to define some standards for the exercise of the discretion conferred by Section 4909.15(A)(1) Revised Code is unfounded (*Ohio Edison Company, supra*). Intervenors' specific objection to the inclusion of Project No. 1974 IBM, applicant's share of Unit No. 3 at the Bruce Mansfield generating station, does warrant some comment. This item constitutes some $90 million of the total allowance requested and there is no dispute that the project meets all the statutory eligibility criteria (App. Ex. 1, Sched. B-4). However, in keeping with their assertion that the company already has excess generating capacity and their opinion that applicant has demonstrated no compelling financial need, the City of Cleveland and Senior Citizens, *et al.*, urge the Commission

to ignore this substantial capital investment in establishing rates in this case. Given our perception of the purpose of the statutory provision allowing consideration of construction work in progress as explained in *Columbus and Southern Ohio Electric Company,* Case No. 77-545-EL-AIR (March 31, 1979), and recently reiterated in *Ohio Edison, supra,* we would think that there would be less room for argument concerning the propriety of including Mansfield Unit No. 3 than any other of the items for which applicant has requested recognition. In light of the Commission's rejection of intervenors' excess capacity theory and consistent with our prior holdings with respect to proposed "overwhelming need" standards, the Commission overrules these objections (*Dayton Power and Light Company,* Case No. 76-823-EL-AIR [July 22, 1977]; *Cleveland Electric Illuminating Company,* Case No. 78-677-EL-AIR [May 2, 1979]).

As indicated above, the difference in the applicant and staff construction work in progress recommendations is relatively minor, and part of the remaining disparity is attributable to the difference in the allocation methods employed. Yet despite the comparatively small total dollar difference between the respective proposals, there are some 76 individual job orders still in dispute (S.R., p. 25). The basis for applicant's objection to the staff exclusion for each of these items is set out in the testimony of applicant's witness Kemper (App. Ex. 3A, pp. 10-28). Given the obvious constraints which preclude the Commission from proceeding with an individual analysis of each one of these job orders within the confines of this written opinion, we believe it reasonable to resolve the matter through a more general discussion. In light of the fact that the Commission has previously indicated that it believes the purpose of the allowance to be to recognize the existence of major new construction projects, it is tempting to simply eliminate a number of these items as not constituting the type of evidence contemplated by the

statute. However, the staff has inspected each of these items and has offered additional reasons why they should not be considered (Staff Ex. 1, pp. 3-18). Nothing in this record would persuade us that the allowance recommended by the staff is unreasonable.

Applicant begins its criticism of the staff's findings by suggesting that the Commission should, as a matter of policy, recognize in the allowance any expenditures relating to efforts to improve power plant productivity or required by various governmental agencies for environmental or safety reasons (App. Ex. 3A, p. 9). The unfortunate negative implication of this recommendation is that if the Commission fails to adopt these criteria it is unconcerned about applicant's productivity, the environment, or the public safety. We trust that all concerned will recognize this smoke screen for what it is and will realize that the real issue here is whether or not the expenditures represent qualifying construction projects under the statute and our past decisions.

Review of the testimony of staff witness Weiss indicates that the reasons underlying the staff's exclusion of the projects now in issue fall in four basic categories (Staff Ex. 1, pp. 3-18). Some were excluded because the staff found them to be less than 75 percent complete. Several were eliminated upon a finding that they represented a purchase rather than a construction project. Others were excluded because they were of a replacement nature. Finally, there were exclusions based on the conclusion that the expenditures involved were more properly associated with maintenance rather than construction. In several instances the exclusion, was tied to more than one of these reasons. Each one of the identified criteria has been recognized by the Commission in past cases as representing an appropriate standard by which to test the eligibility of specific expenditures for inclusion in the construction work in progress allowance (S.R., p. 25). Moreover, the Commission has also pointed out that there is

judgment involved in applying every one of these tests. Despite the complaints from those who would have the Commission establish rigid rules to be strictly applied in every case, we continue to believe that judgment must play an important role in determining what evidence is properly considered in authorizing an allowance for construction work in progress in a given case.

For purposes of illustration, consider the Commission's determination that items which constitute purchases are not construction projects within the meaning of the statute. The logical foundation of this standard is so clear that an explanation is almost superfluous. An item acquired by a utility through a single-payment transaction is either in service at date certain and, therefore, in rate base, or it is not, and no return may be earned on it. A purchase is not construction, nor is it a project. Applicant's job order no. 50030, a caterpillar tractor-scraper acquired for use at one of the company's power plants, is a clear-cut example of a purchase (App. Ex. 3A, p. 23). It was properly excluded by the staff (Staff Ex. 1, p. 14). But compare this situation to job order no. 50228, a crawler tractor purchased and delivered prior to date certain but which required additional company labor before it was ready for use (App. Ex. 3A, p. 22; App. Ex. 3B). Does this change its essential nature from a purchase to a construction project? The Commission would agree with the staff conclusion that it clearly did not (Staff Ex. 1, p. 13), but there is now an element of judgment involved.

This same element of judgment is also present to some degree in each of the other tests the staff employed. The staff's finding that several of the job orders proposed for inclusion by applicant were not 75 percent complete followed from the staff's opinion that these items, because of their scope and purpose, should be examined individually and not considered as a part of a larger project as the company had suggested (Staff Ex. 1, p. 7). The exclusion

of items on the ground that they represent replacement projects or maintenance work also requires that a view be taken as to the basic characteristic of the expenditure (See *Toledo Edison Company*, Case No. 79-143-EL-AIR [February 29, 1980]). In each instance, the Commission believes the treatment recommended by the staff to be consistent with the intent of the statute and, therefore, finds that the construction work in progress allowance proposed by the staff should be adopted for purposes of these proceedings. Those items excluded are not properly defined as major new construction when the amount of the obligated capital involved is considered in connection with time period for which it has been committed and the purpose to which it has been put. Applicant's objection is overruled.

Working Capital:

The applicant, the staff, and Consumers' Counsel each proposed an allowance for working capital to be included in the rate base valuation in accordance with the provisions of Section 4909.15(A)(1) Revised Code. All three estimates were derived through the use of the formula approach, but there are significant differences between the results of the respective calculations. Applicant requests an allowance of $128,393,775 (App. Rev. Sched. B-1), while the staff's recommended allowance is $62,865,000 (Staff Ex. 7, Rev. Sched. 7). Consumers' Counsel's calculation resulted in a proposed allowance of $56,935,000 (O.C.C. Ex. 1, Rev. Sched. JTC-2). Issues exist with respect to each element of the formula which we will address, in turn, below.

The difference in the cash component of the formula as presented by the parties is, in part, the product of the sponsors' respective positions on various expense issues and, in some measure, created by the difference in allocation methods. The most significant difference, however,

arises from the fact that the applicant failed to exclude fuel expense from operation and maintenance expenses in computing its proposed cash allowance. Staff witness Hanna and Consumers' Counsel witness Chapski both believe this deduction to be appropriate (Staff Ex. 7, p. 12; O.C.C. Ex. 1, pp. 12-13). Much of the debate on this point has centered on applicant's complaint that fuel expense was not deducted under the original formula as propounded by the FPC (now FERC) (App. Brief, p. 12). Be that as it may, it is clear that this Commission has consistently excluded fuel expense under its version of the formula for some years, and, in most instances, without objection from the utility involved (See, *e.g.*, *Ohio Edison Company*, Case No. 78-1567-EL-AIR [January 30, 1980]). The Commission has cited as one of the virtues of the formula method for determining a working capital allowance that it assures evenhanded treatment among rate applicants (*United Telephone Company of Ohio*, Case No. 72-995-Y [September 9, 1974]). It has never suggested that the formula does more than approximate the result of a full-blown lead-lag study. If applicant wishes to depart from this formula on the grounds that it does not properly recognize one item or another, we suggest that it support this claim with a properly conceived lead-lag study which examines all the timing differences involved between when expenses are incurred and payments are received. Applicant's objection is overruled.

The applicant and the staff utilized the date certain balance for purposes of determining the materials and supplies component of the working capital formula. Consumers' Counsel witness Chapski used the average of thirteen monthly balances in arriving at his recommendation with respect to this component, a technique approved by the Commission on numerous past occasions, including this company's last rate case, on the grounds that it may

produce a more representative allowance. The staff has indicated that one of the reasons it utilized the date certain balance in this case was that actual test-year data was not available at the time of its audit (Tr. XXI, pp. 174-175). This data is now available to the Commission through Senior Citizen's Ex. 10, and the Commission concludes that the thirteen monthly balance method may properly be the adopted utilizing the information contained therein. Jurisdictional materials and supplies calculated on this basis total $19,034,217. This amount must then be adjusted to eliminate those materials and supplies held for new construction, extensions and additions in accordance with the decision of the Supreme Court in *City of Cincinnati v. Public Utilities Commission*, 160 Ohio St. 2d 395 (1954), and the consistent practice of the Commission in implementing that decision. Applicant objects to this adjustment, claiming that the materials and supplies inventory is not maintained with a view as to the ultimate purpose to which individual items may be put (Tr. II, p. 83). This may well be true, but it certainly does not preclude an after-the-fact analysis of the use to which the items are actually put (S.R., Sched. 11A). The Commission finds the staff adjustment to account for this consideration to be reasonable and proper in all respects. Application of this adjustment factor to the inventory as determined above produces an allowance for materials and supplies of $16,491,246 which we deem reasonable for purposes of determining the working capital allowance to be authorized in these proceedings.

The fuel inventory allowance is composed of three separate items: oil, coal, and deferred nuclear fuel. Differences exist in each of these areas. Applicant based its proposed allowance for oil on a targeted capacity supply level of 90 percent (App. Ex. 5A, p. 13). The staff and Consumers' Counsel are in general agreement that 78 percent of capacity represents a more reasonable inventory

level in light of the company's actual experience (S.R., p. 25; Staff Ex. 6, p. 7; O.C.C. Ex. 1, p. 11). Applicant's witness Chopp was unable to explain the derivation of the the 90 percent target, nor was he aware if 90 percent of tank capacity had ever actually been achieved (Tr. II, pp. 98-100). It was certainly not achieved in the test year. Under these circumstances, the Commission believes the staff's proposed allowance for the oil inventory is on much firmer footing, and we will accept the staff's recommendation with respect to this component of the fuel inventory allowance.

The determination of the proper allowance for the coal inventory has been a subject attended by considerable debate in these proceedings. Applicant originally based its proposed allowance on the assumption that a 63.33-day supply represented a reasonable inventory balance (App. Ex. 5, pp. 16-17). This number was derived through what can only be described as a rather primitive analysis based on the assumptions that the company maintains a 50-day supply in a normal year and a 90-day supply during a year in which a UMW contract is up for renewal. As the miner's contract runs for a three-year period, the calculation assumed two years at the 50-day level and one year at the 90-day level producing a weighted average of 63.33 days. Cross-examination by counsel for Senior Citizens, *et al.*, quickly pointed up the flaw in this logic, as it is apparent that even if one accepts the validity of the general approach, a 90-day supply would not be maintained throughout the third year, but would gradually be built up in anticipation of a possible strike and would dissipate as the threat of the strike passed or as the reserves were called on in the event a work stoppage actually occurred. Mr. Chopp conceded the point (Tr. III, pp. 55-57). This prompted applicant to revise its calculation, this time assuming a 50-day supply in the first two years and a gradual build up and decline in the third year. The resulting weighted average became 55.3 days (App. Ex. 5G), and, based on this

calculation, the company now claims a 55-day coal inventory to be a reasonable basis for establishing the coal allowance. Rather than engage in this speculation, both staff witness Hefner and Consumers' Counsel witness Chapski pegged their recommended allowances to the actual experience of the company. Mr. Hefner, based on date certain data, a review of the monthly balances, and consideration of applicant's budget as it related to coal procurement concluded that a 45-day supply was reasonable (S.R., p. 25; Staff Ex. 6, pp. 6-7; Tr. XXI, pp. 48-49). Mr. Chapski simply relied on the average of the thirteen monthly balances, December, 1978, through December, 1979, in arriving at his recommended allowance which is slightly below that proposed by the staff in terms of actual dollars (O.C.C. Ex. 1, p. 11).

Applicant challenges the conclusions of these witnesses on several counts. The company argues that the use of test-year data is inappropriate, asserting that coal inventory levels in 1979 were lower than normal due to uncertainties arising from questions as to what low sulphur-high sulphur coal mix would be permitted (App. Ex. 5A, p. 14) and due to the fact that the current UMW contract was only in its second year. Applicant presented an exhibit showing that the monthly balances from the three-year period 1976 through 1978 averaged 55 days (App. Ex. 5B). However, when the 1979 data is added to this table a somewhat different picture emerges (Tr. VI, pp. 69-70). Although applicant claims that test-year inventory levels were lower than normal, the 1979 average of the monthly balances, 37.4 days, is actually higher than the 1978 average of 36.5 days (App. Ex. 5B). These numbers are both quite different from the 50-day supply applicant contends should be associated with the years where no strike is imminent. Certainly a plausible interpretation of this data is that the company considered the inventory remaining at the conclusion of the strike in March of 1978 to be reasonably adequate under the circumstances. If one employs appli-

cant's three-year weighted average approach using actual data rather than the assumed inventory levels utilized by the company, the results confirm the reasonableness of the staff's recommended allowance. The average monthly balance for 1977, the year of the strike, constituted a 66.3-day supply. Adding this to twice the 1978 average of 36.5 days and dividing by three yields a 46.4 day supply, a far better match with the staff's 45-day supply than with the company's 55-day recommendation.

Applicant's witness Chopp described the 45-day supply recommended by the staff as being "dangerously close" to the 40-day level specified by the Commission in Case No. 77-1139-EL-COI as the point at which the Company is permitted to abandon economic dispatch (App. Ex. 5A, p. 14). Taken at face value, this might be cause for concern; but the fact is that the company never had a 40-day monthly balance from March of 1978 through July of 1979 (App. Ex. 5B). As the staff points out on brief, the 40-day trigger becomes important only during the period of a strike where all utilities face the threat of service interruption (Staff Brief, p. 6). The Commission concedes that the 45-day supply recommended by the staff appears conservative in light of our findings in other recent electric cases, but we believe the staff recommendation to be the best supported on this record and will adopt the staff's proposed allowance for the coal inventory.

The remaining fuel-related issue to be considered is the appropriate allowance for deferred nuclear fuel. There are two separate questions in this area which must be resolved. Under the leasing agreement between the owners of Davis-Besse and the lessor of the nuclear fuel for the plant, applicant was required to begin payments for nuclear fuel in November 1976, whether or not the plant was in operation (App. Ex. 5A, p. 11). This plant actually was not placed in service until almost a year later, and additional time elapsed before final approval from the Nuclear Regulatory Commission to operate it at full load

(App. Ex. 5A, p. 12). The jurisdictional value of the investment in the fuel core is, of course, properly included in the working capital allowance. This balance is subject to reduction as payments are made to the lessor. Proper accounting dictates, however, that the nuclear fuel be expensed at the time when the fuel is consumed, even though the lease payments are actually made monthly under the terms of the contract (App. Ex. 5, p. 10). Thus, those payments made prior to the commercial operation of the plant are being amortized over the actual fuel burn-up (App. Ex. 5, p. 15). Applicant charged AFUDC on the payments made during this period (App. Ex. 5A, p. 12). The staff recommends that this AFUDC component, $228,835, be eliminated for purposes of determining the working capital allowance, contending that AFUDC was not properly chargeable on these payments as they do not represent construction costs of the type subject to AFUDC accumulation (Staff Ex. 7, p. 21; Staff Ex. 3, Rev. Sched. 11). The Commission agrees that this component should be eliminated. In so finding, we do not in any way suggest that applicant acted imprudently in entering into the leasing arrangement at the time it did, but we do not believe it consistent with the concept of a reasonable working capital allowance to charge ratepayers with these additional costs. Applicant's objection is overruled.

The applicant and the staff relied on the date certain balance for purposes of determining the allowance for deferred nuclear fuel (App. Ex. 1, Sched. B-5.1; Staff Ex. 3, Rev. Sched. 11). Consumers' Counsel used the average of thirteen monthly balances, which produced a somewhat lower figure (O.C.C. Ex. 1, p. 11). Senior Citizen's *et al.*, objects to these methods, arguing that they improperly charge ratepayers for increases in the balances caused by the extended outage of Davis-Besse in the late spring and early summer of last year (Senior Citizens Brief, pp. 9-10). As explained above, because nuclear fuel is expensed only when it is actually consumed, the balance will increase

under the operation of the lease in those periods when Davis-Besse is not on line. As intervenor correctly observes, the date certain balance is the second highest of the test-year monthly balances (App. Ex. 5E). As other aspects of test-year operations have been normalized so as to protect ratepayers from charges attributable to the unit's poor performance, we see no reason why the allowance for deferred nuclear fuel should not be accorded similar treatment. Applicant's witness Chopp agreed that there was no theoretical difference between such an adjustment and those made in other areas (Tr. VI, pp. 67-68). The evidence now before us will not permit the Commission to precisely calculate such an adjustment, but we believe a reasonable proxy for a normalizing adjustment of this type to be to establish the allowance for deferred nuclear fuel with reference to the average of the thirteen monthly balances adjusted so as to eliminate the three months of the TMI-related shut down (App. Ex. 5E). The results of this calculation produce a jurisdictional average of the ten remaining monthly balances of $7,013,586. The Commission is of the opinion that this represents a reasonable allowance for deferred nuclear fuel.

The largest single cause of the disparity between the applicant's working capital recommendation and that proposed by the staff and Consumers' Counsel stems from the fact that applicant failed to include an offset to the working capital allowance to reflect the availability of accrued taxes as required by the decision of the Supreme Court in *Cleveland Electric Illuminating Company v. Public Utilities Commission*, 42 Ohio St. 2d 403 (1975). Applicant has presented nothing new in support of its objection to the offset; in fact, it has presented almost nothing at all. Consumers' Counsel's objection that the offset should include FICA taxes has also been disposed of by prior Commission decisions (See *Columbus and Southern Ohio Electric Company*, Case No. 77-545-EL-AIR [March 31, 1978]). The tax offset proposed by the staff is hereby approved.

The final area of disagreement relates to the deduction for customer deposits required by the decision of the Supreme Court in *Consumers' Counsel v. Public Utilities Commission*, 58 Ohio St. 2d 108 (1979). Applicant, consistent with its apparent theory that precedent should be ignored if it works to the company's disadvantage, made no such deduction. The staff, in accordance with prior Commission decisions, treated the jurisdictional customer deposit balance as an offset to working capital, while Consumers' Counsel contends that it should be subtracted directly from rate base. As the Court indicated in the *Consumers' Counsel* decision, *supra*, the practical effect of either technique is the same. The Commission finds the deduction of $833,000 proposed by the staff to be appropriate, and will express the deduction as a working capital offset for purposes of these proceedings.

The following schedule presents in summary form the Commission's determination of the allowance for working capital to be included in rate base for purposes of these proceedings. These figures take into account revisions necessary to reflect the disposition of those other issues which affect the allowance.

Jurisdictional Working Capital Allowance
(000's Omitted)

Cash Element (⅛ of Adjusted Operation and Maintenance Expense, excluding Fuel and Purchased Power)	$ 20,335
Materials and Supplies	16,491
Fuel Inventory (Including Deferred Nuclear Fuel)	47,012
Tax Offset (¼ of Adjusted Taxes, excluding FICA and deferred FIT)	(20,480)
Customer Deposits	(833)
Jurisdictional Working Capital Allowance	$ 62,525

Accumulated Deferred Taxes and Tax Credits:

In every rate order issued since interperiod tax allocation became permissible under Section 4909.15(A)(4) Revised Code, this Commission has reduced the rate base of normalizing utilities by an amount equal to the balance of accumulated deferred taxes and tax credits which may be deducted without loss of benefit under the applicable provisions of the Internal Revenue Code. Although this practice is consistent with the customary regulatory treatment of these items throughout the country (Tr. XI p. 3), the Commission continues to be subjected to theories advanced by applicant utilities as to why such an adjustment is improper or inappropriate. Mercifully, the barrage has slowed somewhat of late, and in this case applicant has primarily directed its objection to the amount of the deduction rather than to its propriety.*

The staff proposes a reduction to rate base in an amount equal to the date certain balance of jurisdictional accumulated deferred income taxes associated with liberalized depreciation (Account 282) and accelerated amortization (Account 281), and the date certain accumulated deferred investment tax credits (Account 255, 3 and 4 percent components only). (S.R., p. 26). The total deduction is $79,215,257 (S.R., Sched. 12). Applicant also reduced rate base to reflect these balances, but restricted its origi-

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* Applicant did again raise the now familiar "Congressional intent" argument considered and rejected by the Commission in the company's last rate case (Case No. 78-677-EL-AIR [May 2, 1979]). The Commission has no quarrel with applicant's interpretation that the tax credits involved were authorized to provide an incentive for capital investment; but the rate base deduction is not inconsistent with that intent (Staff Ex. 7, pp. 27-28). Congress has specifically indicated those circumstances under which a rate base deduction is not permitted without loss of the benefit, and the Commission has made no adjustment in those instances (Section 46(f), Internal Revenue Code).

nal adjustment to some 44 percent of that proposed by the staff based on a purported identification of the risk-related portion of the deferred amounts (App. Ex. 1, Sched. B-8; App. Ex. 4, pp. 45-48). Through his supplemental testimony, applicant's witness Maugans now proposes an even more limited reduction based on the theory that only the deferred amounts actually recovered through rates may properly be deducted from rate base (App. Ex. 4A, Appendix 6; App. Ex. 4A, pp. 33-38). The Commission finds neither of these arguments persuasive.

Able cross-examination by staff counsel made short work of the novel concept that a risk differential exists with respect to a portion of the deferred balances and credits which dictates that they be included in rate base (Tr. XI, pp. 2-33). Mr. Maugans apparently concedes that the accumulated deferrals represent interest-free capital and, as such, may properly be deducted from rate base (Tr. XI, p. 20). However, the witness then draws a distinction between the terms "interest-free" and "risk-free" in arguing that a return should be allowed on a portion of the balances (Tr. XI, p. 20). The risk to which Mr. Maugans makes reference in the risk that the ultimate tax liability associated with the deferrals will not be paid. This risk is so obviously a risk to the federal government as opposed to one borne by the investors that this matter merits no further discussion. Indeed, applicant has abandoned the argument on brief.

The alternative deduction presented through Mr. Maugan's supplemental testimony is based in language appearing in the Commission's decision in *Ohio Power Company*, Case No. 78-676-EL-AIR (April 16, 1979) to the effect that a determination must be made as to whether existing rates reflect normalization before a rate base reduction for deferred taxes can properly be made (App. Ex. 4A, p. 35). In light of this statement, Mr. Maugans attempted to calculate the portion of the deferred balances

which had actually been recovered through past rates and concluded that a rate base deduction of no more than $25,687,045 was appropriate (App. Ex. 4A, p. 37). Although there are very real problems presented by the assumption that the amount of the recovery through past rates can actually be identified, the Commission need not consider this point in view of our conclusion that applicant's reliance on the language cited is misplaced. First, the Commission would point out that the discussion in *Ohio Power, supra,* related solely to the question of the appropriate treatment of deferred taxes associated with Ohio Electric Company, a subsidiary of Ohio Power whose rates had not theretofore been subject to Commission review. Secondly, whether or not one believes the issue in that case to have been correctly decided, it is quite clear from other orders addressing this subject that the Commission has viewed the controlling factor to be that these deferred amounts are not investor-supplied sources of funds, without real concern as to whether they are theoretically provided by customers or by the federal government. In fact, in the very first rate decision following statutory authorization of normalization, the Commission approved a rate base deduction (*Dayton Power and Light Company,* Case No. 76-88-GA-AIR [July 22, 1977]). Certainly there had been no actual customer "funding" of the deferrals at that time. In essence, the deferrals operate as a continuing offset to the original cost of the property with which they are associated and should be so considered for rate-making purposes. The Commission is of the opinion that Section 4909.05(I) Revised Code contemplates this type of rate base adjustment, but even if in the absence of express statutory authority we would view the staff's deduction as an appropriate and necessary adjunct to our approval of interperiod tax allocation. Applicant's objection should be overruled.

Rate Base Summary:

In light of the foregoing discussion, the Commission finds the jurisdictional rate base as of the date certain of June 30, 1979, to be as set forth on the following table. This table also presents the Commission findings as to rate base properly attributed to the application area and the City of Cleveland under the staff's allocation methodology which we have heretobefore approved.

Rate Base Summary
(000's Omitted)

	Total Jurisdiction	Application Area	City of Cleveland
Plant In Service	$1,876,953	$1,302,137	$ 574,816
Depreciation Reserve	(466,049)	(323,352)	(142,697)
Net Plant In Service	$1,410,903	$ 978,784	$ 432,119
CWIP	91,521	62,976	28,545
Working Capital	62,525	43,619	18,906
Deferred Taxes and Tax Credits	(79,216)	(54,514)	(24,702)
Rate Base	$1,485,734	$1,030,866	$ 454,868

OPERATING INCOME

Applicant and the Commission's staff each submitted an analysis of test-year accounts reflecting the results of operations under the company's present permanent rates. Consumers' Counsel also submitted evidence in support of proposed adjustments to the staff's findings and several intervenors have challenged certain of the results of the staff audit through their filed objections. A number of the issues presented are identical to those heard and decided in the company's last rate case (*Cleveland Electric Illuminating Company*, Case No. 78-677-EL-AIR [May 2, 1979]),

as are the arguments advanced in support of the competing positions. The Commission sees no purpose to be served by another detailed analysis of these same questions and, where appropriate, will merely indicate that our determination is in accord with our prior decision.

Operating Revenue:

The staff found applicant would have realized gross annual operating revenues of $773,389,000 had its present permanent rates been in place throughout the test year (Staff Ex. 3, Rev. Sched. 1). Although applicant originally raised a number of issues with respect to the staff's revenue determination through its filed objections, revisions offered by the staff at hearing have served to remove most of these matters from controversy (Staff Ex. 3; Staff Ex. 4; Staff Ex. 7). The applicant and the staff now agree with respect to the annualization of fuel costs and revenues and this question requires no further review. Applicant will be directed to file base (or non-fuel) rates sufficient to compensate the company for the approved allowable expenses, exclusive of fuel costs includable under Rule 26, and yield the authorized return on rate base, based on test-year operations as analyzed herein (*Dayton Power and Light Company*, Case No. 78-92-EL-AIR [March 9, 1979]).

An issue does remain, however, with respect to applicant's proposal to amortize the revenue and expense impact of a change in the demand charges contained in the contract governing purchases from Ohio Power Company (App. Ex. 1, Sched. C-3.21; App. Ex. 7A, pp. 2-3). The staff recommends against such an adjustment, pointing out that the change, which became effective January 1, 1980, is out-of-period, and that the annualization of purchased power costs, even to year-end levels, has not been considered appropriate by the Commission (Staff Ex. 7, pp. 36-37). The staff also explains that the specific change

in the Ohio Power contract relates to short term and limited term purchases, many of which will be recovered through the fuel adjustment clause (Staff Ex. 7, p. 37). As the Commission found in our recent decision in *Toledo Edison Company*, Case No. 79-143-EL-AIR (February 29, 1980), the month-to-month and year-to-year fluctuations in purchased power expense may occur for a variety of reasons and there is no assurance that an annualizing adjustment of the type proposed by applicant will render purchased power expense any more reflective of future conditions than reliance on the test-year figures. Further, allowable purchased power costs under the fuel adjustment clause cannot be predicted because of the multitude of complex factors which govern recovery through that mechanism. Applicant's proposed adjustment does not adequately consider this point (Staff Reply Brief, p. 8). The Commission will accept the staff's recommendation in this regard.

Labor Expense:

There are several issues in these proceedings which fall under the general heading of labor expense. Specifically, they involve the annualization of union wage increases, the annualization of non-union wage increases, and the annualization of overtime expense. The staff annualized union and non-union wage increases in place at the conclusion of the test year, but did not annualize the effect of any increases in the overtime rate (S.R., Sched. 3.4). Applicant annualized union wage increases through the May 1, 1980 contract, and non-union and overtime through the completion of the test year (App. Ex. 1, Sched. C-3.4). Consumers' Counsel objects to the annualization of any non-union wage increases.

The Commission has addressed each of the issues presented in a number of its recent decisions. For purposes

of these proceedings, we accept the staff adjustment for union and non-union increases in accordance with our decisions in this company's prior case and in *Toledo Edison Company,* Case No. 79-143-EL-AIR (February 29, 1980). We reject applicant's annualization of the May 1, 1980 increase as it does not comply with the standards for such a post-test period adjustment as set out in *Columbia Gas of Ohio,* Case No. 77-1309-GA-AIR (May 24, 1979) and *Cincinnati Gas and Electric Company,* Case No. 79-11-EL-AIR (January 7, 1980). Although the per unit rate of the increase may be known with certainty, there is no assurance that changes in number of employees, budgeted hours, and employee mix will not lead to an overstatement of the costs properly matched with that level of service and productivity experienced during the test year (See *Columbia Gas of Ohio,* Case No. 76-704-GA-CMR [June 29, 1977]). We do find, however, that applicant has satisfied the requisites of *Dayton Power and Light Company,* Case No. 79-372-GA-AIR (May 7, 1980), with respect to its proposed annualization of overtime expense, and that adjustment should be approved. Pension costs will be adjusted to reflect the above findings.

Power Plant Maintenance Normalization:

The applicant and the staff both adjusted power plant maintenance expenses to reflect the deferral of maintenance originally scheduled for the first half of the test year to future periods due to the extended shut-down of Davis-Besse during the second quarter of 1979 (App. Ex. 1, Sched. C-3.11; S.R., p. 14; S.R., Sched. 3.12). The staff adjustment normalized maintenance only to the extent budgeted maintenance was pushed into the second half of the test year. Applicant's adjustment recognized maintenance deferred into 1980. The purpose of this adjustment is to establish a reasonable annual allowance for

power plant maintenance. The Commission agrees with applicant that the staff adjustment fails to recognize the level of maintenance which would have been performed during the test year but for the unusual outage. The deferral of maintenance for the first half to the second half of the year meant that maintenance planned for the latter period had to be deferred until some subsequent time as maintenance schedules had become filled (App. Ex. 5A, pp. 22-24). Applicant's adjustment should be approved and its objection to the staff adjustment is, hereby, sustained.

Vehicle Fuel Annualization:

In recognition of the extraordinary increases in the cost of fuel used in company vehicles, the staff annualized vehicle fuel prices to year-end levels (S.R., Sched. 3.7). Applicant also proposes an annualizing adjustment to vehicle fuel; but would have the Commission calculate the adjustment with reference to March, 1980 price levels (App. Ex. 1, Rev. Sched. C-3.8; App. Ex. 5A, p. 21). Our earlier discussion with respect to annualizations based on post-test year data is dispositive of this issue as well. The Commission is, of course, aware that gasoline prices have continued to rise after the close of the test year. However, an annualization based on some post-test year price level ignores what the company's response to this post-test year increase might be. The matching principle may be violated. For example, in this instance applicant's witness Chopp acknowledged that the company was undertaking programs to reduce fuel consumption in an effort to offset these increased costs (Tr. II, p. 110). One would not reasonably anticipate that even the company's most stringent conservation program would totally offset the rise in prices; but the point is that there is no way to measure what the actual effects may be. Thus, although the cost

change may be known and measurable, an element of speculation remains. The Commission overrules applicant's objection to the staff's adjustment.

Storm Damage and Tree Trimming Expense:

As in applicant's prior case, the staff normalized storm damage and tree trimming expense to assure that the rates set in these proceedings would reflect a representative allowance for these items (S.R., p. 14; Staff Ex. 3, Rev. Sched. 3.13 and 3.14). The staff method, which was essentially the same as that approved in the last case, was based on an average of the annual expenses incurred for these items for the previous five years, restated to 1979 dollars. Applicant objected to the staff adjustments and offered alternative calculations based on essentially the same method rejected in the last case. Applicant contends that the staff's adjustment fails to recognize that there has been an actual increase in the amount of work being done; but the company has offered little in the way of conclusive proof that this alleged increase has, in fact, occurred (Staff Reply Brief, p. 14). Consistent with our decision in applicant's prior case, the Commission again finds the staff adjustments to be proper.

Ordered Load Research Expenses:

Applicant proposed an adjustment to test-year expenses to reflect costs associated with load research activity it is compelled to engage in under the provisions of the Public Regulatory Policies Act of 1978 (App. Ex. 1, Sched. C-3.10). The staff recommends that this adjustment be rejected (S.R., p. 18). This expense of $72,084 relates to certain load meters which applicant leased after the close of the test year. The staff's opposition to the adjustment is based not only on the fact that no costs were incurred in the test year, but also on its observation that while the transaction is treated as a lease for purposes of this adjust-

ment, it will be treated as a purchase and capitalized when the property is actually acquired (S.R., p. 14). The Commission agrees that the adjustment should be disallowed.

Advertising Expense:

The staff reviewed the advertising expenses included in applicant's test-year operating expenses and concluded that no adjustment was required based on its view that the company's advertisements conformed to Commission guidelines and PURPA standards (S.R., p. 15). However, at hearing, Consumers' Counsel and Senior Citizens, *et al.*, presented a series of exhibits which contained the copy of advertisements placed in various media by the Illuminating Company during the test year (O.C.C. Ex. 6; Senior Citizens Ex. 11). These adds are clearly promotional and of no benefit to the consumers. In general, the only information they impart is a general observation that although the cost of service has risen over the years, electricity still represents a good value. As calculated from exhibits indicating the test-year expense associated with these ads, their jurisdictional cost was $238,617 (O.C.C. Ex. 7, Senior Citizens Ex. 12). This amount should be eliminated from allowable expenses. The Commission can anticipate applicant's objection to this adjustment. It will be based on the argument that no witness offered testimony that the advertising was promotional in nature or did not benefit consumers. Our response will be borrowed from another source. We know it when we see it.

Charitable Contributions:

As fully explained in the Commission's decision in the company's last rate case, the Illuminating Company does not generally contribute directly to charity, but makes its donations through the vehicle of the CEI Foundation. However, in the course of its investigation the staff did discover some $18,352 that the company had charged to

jurisdictional operation and maintenance expense which the staff believed should be reclassified as a charitable contribution (S.R., p. 15; S.R., Rev. Sched. 3.17). Applicant explained that it had elected to treat this amount as an expense for fear that if it made the donations through the CEI Foundation it could be subjected to penalties if the IRS perceived an indirect benefit to the company (App. Ex. 5A, p. 25; Tr. II, p. 115). The Commission is not particularly concerned as to what treatment the company accords this amount for tax purposes; but for ratemaking purposes it is clear that it should be considered as a charitable contribution. Applicant's objection to the reclassification is overruled.

This Commission has consistently approved a reasonable allowance for charitable contributions in its cost of service analyses and was prepared to do so again in these proceedings. However, the opinion just issued by the Supreme Court in *City of Cleveland v. Public Utilities Commission*, S.Ct. Case Nos. 79-1158 and 79-1173 (July 9, 1980), 63 Ohio St. 2d(1980), quite clearly reverses the Court's recent decision in *City of Cincinnati v. Public Utilities Commission*, 55 Ohio St. 2d 168 (1978), which specifically approved this long-standing Commission practice. In accordance with this new decision, the Commission now finds that the intervenors' objections to any allowance for charitable contributions should be sustained. As the Commission would have accepted the staff's method of calculating an allowance for charitable contributions as we did in the prior case, the effect is to reduce allowable expenses from what we would have otherwise determined by the amount of $492,539 (S.R., Sched. 3.18).

Rate Case Expense:

Contrary to customary practice, the company did not propose an allowance for expenses incurred in connection with these proceedings in its cost of service analysis.

Rather, applicant elected to rely on the rate case expenses actually charged to its books during the test year on the theory that it will be filing such cases on an annual basis (App. Ex. 5A, pp. 26-27). The staff did obtain an estimate of the costs anticipated by applicant in connection with these proceedings (App. Ex. 1, Sched. C-9), made a determination that the estimate was reasonable, and recommended that the estimated expense be amortized over a two-year period. Thus, the staff's proposed allowance is $174,000 (S.R., Sched. 3.19). Upon review of the record relative to this subject, the Commission believes the staff's proposed allowance should be accepted. The bulk of the rate case expense incurred by applicant during the test year related to its prior case. As a theoretical matter, expenses associated with the prior case should not be built into the rates authorized in these proceedings. Moreover, the Commission is concerned that applicant's proposed method of dealing with this subject may make our review of the reasonableness of these expenditures more difficult. With due regard for our prior observations concerning the nature and purpose of the rate case expense allowance, the Commission sees no reason to depart from our usual practice with respect to this item (See, *e.g., Columbus and Southern Ohio Electric Company,* Case No. 77-545-EL-AIR [March 31, 1978]).

Intervenor City of Cleveland objects to the staff's proposed allowance for rate case expense and a considerable portion of this record is devoted to its attack on the reasonableness of the staff's finding. This onslaught was then broadened to include the question of legal fees in general. Despite the pages of transcript generated by the City of Cleveland's efforts in this regard, there is not one iota of affirmative evidence that the rate case expense allowance is unreasonable or that applicant's practices with respect to retaining legal counsel are inconsistent with that which should be expected from a major corporation

(Tr. XXXI). Further, intervenor never suggested, either through a witness or on brief, what it considered to be reasonable with respect to these areas. All the Commission is left with are its bare assertions that the amounts proposed by the applicant and the staff are not. These objections should be overruled.

PUCO Maintenance Tax and Consumers' Counsel Assessment:

Although it has been the consistent practice of the Commission, applicant objects to the staff's classification of the PUCO maintenance tax and Consumers' Counsel assessment as "other taxes", contending that the Uniform System of Accounts requires that they be charged to operation and maintenance expense (App. Ex. 5A, p. 24). The significance of this issue is, of course, the effect on the working capital calculation. On brief, staff counsel argues that the accounting requirements are not as clear cut as applicant would have us believe and points out that applicant is one of the few utilities that does not account for these items as taxes (Staff Reply Brief, p. 11). Neither of these arguments need detain us, for no matter what method the company elects to employ for bookkeeping purposes, the Commission would still consider the assessments as taxes for ratemaking purposes. Applicant's objection to the staff's classification is overruled, as is its objection that these amounts should be allocated, a matter decided in the company's last case.

Pennsylvania Public Utility Realty Tax (PURTA):

Pennsylvania has enacted a public utility realty tax which significantly increased applicant's tax obligation in that state commencing with the 1979 tax year. As a part of this new law, the Pennsylvania legislature also imposed a one-time surcharge, in applicant's case amounting to approximately $1.4 million, which the company paid dur-

ing the test year. Although both the applicant and the staff recognized the PURTA tax in their calculation of allowable expenses, the staff eliminated the surcharge payment from its cost of service determination (S.R., p. 17; S.R., Sched. 3.24e). Applicant objects to the staff adjustment.

The Commission has had occasion to consider this precise question in its recent decisions in *Ohio Edison Company,* Case No. 78-1567-EL-AIR (January 30, 1980) and *Toledo Edison Company,* Case No. 79-143-EL-AIR (February 29, 1980). Consistent with those decisions, the Commission again concludes that the staff adjustment is, in all respects, reasonable and proper and should be approved. No one disputes that this one-time surcharge is a nonrecurring expense. As such, it should not be reflected in future rates, and applicant's now familiar arguments to the contrary must, accordingly, be rejected. There is no merit in the claim that this nonrecurring expense should be allowed in recognition of the possibility that there may be other nonrecurring expenses in the future, nor is their merit in the theory that disallowing the expense will encourage state legislatures to view the mechanism of a surtax as a source of "free money" (App. Ex. 5A, pp. 30-32). The risk that there will be unanticipated expenses in the future is a risk assumed by the investor when he purchases the company's securities. Indeed, the investor's assessment of this risk plays a big part in establishing his return requirements. Further, a state legislature which intentionally pursued the course hypothesized by applicant would either effectively render what was nominally a one-time surcharge a recurring expense deserving of rate recognition, or would create a climate which would ultimately result in increased investor requirements relative to the affected utilities. Those increased requirements would, in time, lead to increased rates.

On brief, applicant submits that its property "is simply confiscated" by the exclusion of this item from cost of service (App. Brief, p. 16). This is nonsense. As this Com-

mission has repeatedly pointed out, the purpose of rate regulation is not to guarantee the dollar-for-dollar recovery of specific past expenses, but rather to determine a representative allowance for expenses which will provide a reasonable future earnings opportunity (See *e.g., Ohio Edison Company,* Case No. 77-1249-EL-AIR [November 17, 1978]). Applicant suggests that the Pennsylvania legislature imposed this surcharge in order to retain monies collected during the pendency of a challenge to an earlier version of the PURTA tax which eventually resulted in the tax being overturned. (See *Commonwealth v. Philadelphia Electric Co.,* 472 Pa. 530 [1977]). This points up the very reason nonrecurring costs are not considered in fixing future rates. Assume for purposes of discussion that the court decision had been adverse to utility interests and that the tax had not theretofore been considered for ratemaking purposes. The fact that applicant loses sight of in its "confiscation" argument is that building a mechanism for recovery of the surcharge into future rates would have absolutely no effect on the company's 1979 financial performance. The Commission has not denied applicant an earning's opportunity. The expense is history and has no place in the establishment of future rates.

Federal Income Tax:

Through its filed objections, applicant originally took exception to a number of aspects of the staff's federal income tax calculation. Most of these objections were tied to other staff expense adjustments and are now resolved. Of those that remain, applicant pursued only the investment tax credit amortization question on brief. The treatment the staff accorded this item is in keeping with that approved in prior Commission cases, and is the balance of the staff's method. The staff's calculation of federal income tax expense should be accepted for purposes of these proceedings.

Terminated Generating Units:

By an amendment to its original application, applicant seeks Commission approval of an adjustment to allowable expenses which would permit the company to recover its share of the costs associated with the termination of four nuclear generating units pursuant to the CAPCO decision of January 23, 1980, that Davis-Besse No. 2 and No. 3 and Erie Nuclear Unit No. 1 and No. 2 should be cancelled. Applicant's specific proposal is that the expenses incurred to date for these projects, $56,437,000, be adjusted to reflect necessary tax considerations and amortized over a ten-year period (App. Ex. 4A, p. 22; App. Ex. 1, Sched. 3.22). The staff recommends approval of the adjustment (Staff Ex. 11, pp. 18-20; Staff Ex. 7, pp. 37-40). Consumers' Counsel and intervenors City of Cleveland and Senior Citizens, *et al.*, object to any recognition of these termination costs in the rates to be established in these proceedings.

As a preliminary matter, the Commission must first take up intervenors' claim that this issue is not properly before the Commission as the adjustment was not proposed until after the notice of the rate request required by Section 4909.18 Revised Code had been published. The Commission disagrees with these arguments, noting that statute only contains the requirement that "the substance of the application" be noticed. Because applicant did not propose any specific increase in the actual rates requested, the substance of the application is unaffected by this later adjustment to the supporting data. Had the proposal predated the notice, there would certainly have been no requirement that it be included in the publication.

The real threshold question here, which the Commission perceives as the most difficult of all the issues raised in connection with this matter, is whether this adjustment is legally permissible. In reviewing all the available cases considering cancellation costs from both state and federal

regulatory jurisdictions, we find the most surprising feature to be, not the fact adjustments of this type have been approved without exception, but that there is no hint that this legal question was ever even raised (App. Ex. 4A, p. 69). At first blush, one would think that the risks of cancellation should be borne solely by the investor; however, applicant's arguments persuade us that this is not the case (App. Brief, pp. 8-15). Intervenors approach this issue as though it were a rate base question, emphasizing the fact that the terminated units have never and will never provide service to customers. This is quite clearly correct, but it is irrelevant. There is no request by the company that it be permitted to earn a return on this investment, although some jurisdictions have permitted this treatment. What the company seeks is the recovery of costs incurred on behalf of its ratepayers to assure that adequate service could be maintained (Tr. XXI, p. 185). The significant question, given the Commission's past pronouncements with respect to the impropriety of the recovery of past losses through future rates, is whether the amortization of these extraordinary costs does violence to this principle. The distinguishing feature that sets this adjustment apart from those we have rejected on this ground in the past is that costs associated with the termination of the units did not really become costs until the fact of termination. Cancellation does not create a past loss, but gives rise to a current cost. Unlike the PURTA surtax issue discussed earlier, where approval of the proposed adjustment would have had no effect on the company's future earnings opportunity, rejection of this adjustment would have a very direct impact on applicant's financial performance as, in the absence of funding of the amortization through rates, applicant would be required to write off these costs currently (Tr. XXII, p. 49). Thus, we now see the wisdom of the standard emerging from the cases from other jurisdictions; if the expenditures are prudent, amortization should be permitted.

In determining whether these expenditures were prudent, one must bear in mind what is and what is not at issue. No one disputes that the 1973 decision to embark on the construction in question was reasonable as it was based on the best data available (App. Ex. 11; App. Ex. 29; Staff Ex. 11). Similarly, no one disputes that the decision to terminate construction was reasonable, given the intervening decline in growth expectations and the uncertainties which now attend the construction of nuclear units. Thus, the only real question is whether the decision to terminate should have been made sooner. Applicant's witness William described in detail the company's response to changes in growth rates, including postponements of units so that in-service dates would better match the results of new load forecasts (App. Ex. 11, p. 30). Only Consumers' Counsel witness Rosen offered testimony suggesting that the units should have been cancelled earlier (O.C.C. Ex. 5), and his opinion is of doubtful value as it is based solely on CAPCO information and does not specifically address any of the considerations which may have influenced this applicant's decisions (Tr. XXVIII, p. 115; Tr. XXIX, pp. 19-21). Further, the alternative construction program he now recommends for CAPCO, which involves an unbelievable reliance on oil-fired peaking units, casts doubt on the credibility of his entire study, even if it were found to have any application in this case. The Commission finds that applicant's decisions were reasonable and prudent at every step of this process, and concludes that the proposed adjustment should be approved. For purposes of these proceedings we accept the staff's method of calculating the adjustment (Staff Ex. 3; Sched. 3.0).

Operating Income Summary:

Consistent with the foregoing discussion, the Commission finds applicant's jurisdictional adjusted operating income for the twelve months ending December 31, 1979,

the test period in these proceedings, to be as set forth on the schedule below. Although revenues can be directly assigned to the application area or the City of Cleveland, expenses must be allocated. The following schedule also depicts the results of the application of the staff's proposed expense allocation factors which the Commission has accepted as reasonable for purposes of these proceedings:

Adjusted Operating Income
(000's Omitted)

	Total Jurisdiction	Application Area	City of Cleveland
Operating Revenues	$773,389	$542,489	$230,900
Operating Expenses			
Operation and Maintenance	$471,852	$330,775	$141,077
Depreciation Expense	61,277	43,342	17,935
Taxes Other Than FIT	76,194	53,163	23,031
Federal Income Tax	39,355	28,227	11,128
Total Operating Expenses	$648,678	$455,507	$193,171
Net Operating Income	$124,711	$ 86,982	$ 37,729

PROPOSED INCREASE

A comparison of jurisdictional operating revenues of $773,389,000 with the allowable jurisdictional expenses of $648,678,000 indicates that under its present permanent rates applicant realized income available for fixed charges in the amount of $124,711,000 based on adjusted test-year operations. Applying this dollar return to the jurisdictional rate base of $1,485,734 results in a rate of return under present rates of 8.39 percent. Current rates to customers in the application area produced test-year income available of $86,982,000, which, when applied to the allocated rate base of $1,030,866, yields a rate of return of 8.44 percent. Present rates to customers in the City of Cleveland, which

are the same as those contained in the ordinance complained of, resulted in adjusted test-year net operating income of $37,729,000. This dollar return, when applied to the rate base properly allocable to the City of Cleveland of $454,868,000, produces a rate of return of 8.29 percent. All these rates of return are well below that recommended as reasonable by any of the expert witnesses testifying on this subject and the Commission must, therefore, find that the company's present rates are insufficient to provide it reasonable compensation and return for the electric service it renders. Moreover, Ordinance No. 1673-79 of the City of Cleveland, which would continue these rates in effect in that municipality, must also be found to be unreasonable. Rate relief is clearly required, and the ordinance complained of must be modified.

Under the rates proposed by applicant, additional gross annual revenues of $79,795,000 would have been realized based on test-year operations as analyzed herein (S.R., Sched. 1). On a pro forma basis, which assumes necessary expense adjustments calculated in a manner consistent with the Commission's findings, this proposed increase would have yielded an increase in jurisdictional net operating income of $41,301,000 resulting in income available for fixed charges of $166,012,000. Applying this dollar return to the jurisdictional rate base results in a rate of return of 11.17 percent. Net operating income for the application area would be increased to $116,008,000 under the proposed rates, resulting in a rate of return on the rate base allocated to this service of 11.25 percent. For the City of Cleveland, the proposed increase produces pro forma income available of $50,004,000 and a rate of return on rate base of 10.99 percent. Although these rates of return are supported by the opinions of applicant's rate of return witnesses, the jurisdictional rate of return under the proposed rates is above the range recommended as reasonable by the staff witness testifying on this subject. The existing rates

are inadequate; but further examination is necessary before a final determination as to the level of rate relief required can be made.

RATE OF RETURN

Three witnesses offered cost of capital analyses to be considered as evidence by the Commission in establishing a fair rate of return for purposes of these proceedings. The study sponsored by applicant's witness Jeffries concludes that a rate of return of from 11.17 to 11.55 percent is appropriate (App. Ex. 8A, p. 8), and applicant's witness Maugans proposes a nearly identical range (App. Ex. 4A, p. 64). Witness Farrar, testifying on behalf of the staff, determined the overall cost of capital to be between 10.65 and 11.02 percent (Tr. XXIV, pp. 4-5). Although the difference between the company and staff positions lies primarily in the area of the cost of common equity, there are certain other minor issues which the Commission must first address.

Capital Structure:

Each of the witnesses employed the company's December 31, 1979, capital structure in their respective cost of capital analyses. The use of a capital structure which reflects post-date certain developments has been approved by the Commission in a number of recent decisions in an effort to better recognize the cost of capital to the applicant utility which will prevail in the period for which rates are being set. (See, *e.g., Dayton Power and Light Company,* Case No. 78-92-EL-AIR [March 9, 1979] and *Ohio Edison Company,* Case No. 78-1567-EL-AIR [January 30, 1980]). Consistent with those decisions, the Commission finds the use of the December 31, 1979, capital structure to be appropriate. The specific ratios, as calculated by Mr. Farrar, are 46.57 percent long-term debt, 15.01 percent preferred stock, and 38.41 percent common equity (Staff Ex. 11,

p. 21). These percentages differ slightly from those computed by applicant due to the fact that the staff and the applicant used different techniques to adjust for a loss experienced by the company in connection with a reacquisition of preferred stock in 1978 (Staff Ex. 11, p. 3). As applicant acknowledges on brief, the difference in the result is not significant (App. Brief, p. 35). Accordingly, we accept the capital structure proposed by Mr. Farrar as reasonable for purposes of these proceedings.*

Cost of Debt and Preferred Stock:

Each of the rate of return witnesses testifying in these proceedings derived the costs to be assigned the debt and preferred stock components of applicant's capital structure by reference to the actual embedded costs of these senior securities. Despite the fact that its own expert witness specifically testified to the contrary (Tr. XVII, pp. 72-73), applicant continues to suggest, as it did in its filed objections, that the use of embedded costs for this purpose is unreasonable and unlawful (App. Brief, p. 35). Although we agree with applicant that a determination of this issue is certainly not essential in this case, the Commission believes it appropriate to lay this theory to rest at this time.

Section 4909.15(D)(2)(a) Revised Code now requires that the Commission determine a fair and reasonable rate of return for an applicant utility with reference to the

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* Although he presented no independent rate of return recommendation, Consumers' Counsel witness Larkin suggested that the Commission should recognize short-term debt in the capital structure utilized in the cost of capital analysis (O.C.C. Ex. 2, pp. 5-8). Such a step would be inconsistent with Commission precedent and contrary to the specific recommendations of the other witnesses; however, the Commission need not reach this question as Consumers' Counsel has, on brief, now indicated its support of the use of the staff's capital structure for purposes of these proceedings (O.C.C. Brief, p. 4).

embedded cost of debt of the utility in question. As anyone familiar with the 1976 changes in Ohio's ratemaking statutes can attest (Am. Sub. S.B. 94), this provision was inserted in response to the decision of the Supreme Court of Ohio in *Cleveland Electric Illuminating Company v. Public Utilities Commission*, 42 Ohio St. 2d 403 (1975), wherein the Court apparently held that the then-existing statutory framework required that the Commission employ the current cost of debt in its rate of return determination. However, even before the legislative reversal of the *Cleveland Electric Illuminating Company* decision, *supra*, the Commission, in its Entry on Rehearing in *Cincinnati Gas and Electric Company*, Case No. 72-415-Y (October 17, 1975), undertook a careful analysis of the existing precedent which let it to the unanimous conclusion that the use of embedded costs was both theoretically appropriate and legally permissible. We commend this discussion to applicant's attention and point out that its logic is even more compelling now that Ohio rate regulation no longer even arguably involves the fictional reproduction of rate base at date certain.

Applicant contends that even if Section 4909.15(D)(2)(a) Revised Code now specifically requires consideration of the embedded cost of debt in the rate of return determination, the silence of the statute with respect to preferred stock should be construed as evidence of a legislative intent that current costs be employed in connection with this capital component. Although the Commission does not take issue with the principle of construction cited by applicant, the result produced by its application in this setting is so unreasonable that we do not believe it can logically be invoked. As suggested above, a review of the history of this provision clearly indicates that it was enacted to overturn a specific judicial decision, not as a directive to the Commission to alter its consistent practice of relying on embedded costs as the best evidence of the

appropriate cost rates to be assigned the long-term debt and preferred stock components of the capital structure. The Commission's discussion of the embedded cost question in *Cincinnati Gas and Electric Company, supra,* in dispositive of this issue as well. Even in the days of the RCNLD rate base, it was a rare exception when a utility rate of return expert proposed the use of anything other than embedded costs in his determination of the weighted cost of senior securities; and the Commission has certainly never been treated to testimony exclusively advocating current costs for these capital components since Ohio became an original cost jurisdiction.

As indicated above, the Commission has accepted the capital structure proposed by staff witness Farrar. We now further find Mr. Farrar's determination of the embedded cost of debt, 8.19 percent, and preferred stock, 8.30 percent, to be reasonable and adopt same for purposes of the analysis in these proceedings (Staff Ex. 11, p. 3).

Cost of Common Equity:

Determining the cost of debt and preferred stock is, and as explained above, should be largely a mechanical process. The cost of common equity, however, can only be estimated. As the Commission has noted on a number of prior occasions, a variety of valid methods exist for obtaining this estimate, and the fact that the Commission selects the recommendation of one witness over that of another does not mean that any of the recommendations are "wrong," save in those instances where internal inconsistencies render a particular recommendation unacceptable even under the sponsoring witness's own approach. The Commission must, in a necessary exercise of its judgment, select that recommendation it believes to be most reasonable in light of the facts and circumstances of a given case. This task is made even more difficult in this case due to the radical changes in financial conditions experienced from the outset

of the test year through the present time. Indeed, these changed circumstances have prompted each of the witnesses offering testimony on the cost of equity to revise his recommendation.

In his original testimony, filed in September of 1979, applicant's witness Jeffries recommended a return on common equity of from 15.0 to 16.0 percent (App. Ex. 8, p. 30). The range he proposes in the supplemental testimony submitted just prior to hearing is 16.00 to 17.00 percent (App. Ex. 8A, p. 2). Applicant's witness Maugans originally suggested as reasonable a rate of 15.5 percent (App. Ex. 4, p. 70). He now supports Mr. Jeffries' revised recommendation (App. 4A, p. 1). As set forth in the staff report, the staff's original position was that the appropriate cost of equity was in the range of 14.01 to 14.94 percent (S.R., p. 27). At hearing, witness Farrar adjusted this recommendation to reflect more current data and concluded the proper cost of equity was between 14.56 and 15.52 percent (Tr. XXIV, pp. 4-5).

Mr. Jeffries employed several methods in arriving at his original recommendation. He performed a comparable earnings test involving a review of the return on common equity achieved over the past ten years by sixteen electric utilities with bond ratings the same as that of the applicant (App. Ex. 8, pp. 20-21; App. Ex. 8, p. 6; Tr. XVII, p. 29). Based on this analysis, Mr. Jeffries concluded that a rate of return on common of 15.00 percent would be appropriate. In evaluating this recommendation, the Commission observes that at no time in the past ten years has the average return of the sixteen companies studied ever reached 15.00 percent. In fact, in the years since 1974, the year of the oil embargo and general business recession, the achieved return for this group has been well below this figure. In both 1978 and 1979 it was 13.2 percent. Mr. Jeffries explained that in arriving at his recommended return based on this evidence he gave consideration to

recently granted and pending rate increase requests (App. Ex. 8, p. 20); however, the effect of these increases was never quantified.

The disparity between the actual data and the witness' recommendation based on that data is not surprising. Indeed, this discrepancy highlights one of the shortcomings of the comparable earnings method which the Commission has identified in the past (*Columbus and Southern Ohio Electric Company*, Case No. 77-545-EL-AIR [March 31, 1978]). Where the members of the group examined for comparative purposes exhibit depressed market-to-book ratios, a vicious circle will be created if their achieved returns are relied on by regulators in determining the rate of return to be authorized in a given case. On the other hand, the logic of the method breaks down if one first looks to the experience of the group defined as comparable, concludes that the experience is not really suitable as evidence under existing conditions, and then, through an exercise of judgment, attempts to establish a return requirement based on a perception of what the group should be earning. This is not to say that the Commission should totally discount the experience of other comparably-rated electric utilities, but merely to point up the fact that the witness has used a good deal of judgment in deriving an equity return recommendation of 15.00 percent from data which, on its face, would apparently support a much lower number.

Mr. Jeffries also looked to the rate of return on common equity of Standard & Poor's 400 Industrials over the past ten years as a basis for his recommendation (App. Ex. 8, p. 21; App. Ex. 8, p. 30; App. Ex. 8, p. 39). He concluded from an examination of the average return earned by this group in the years 1976 through 1978 that a range of 14.50 to 15.20 percent could be supported, and also indicated that in 1979 the experienced return had jumped to 16.90 percent (Tr. XVII, p. 36). The witness included this broad

industrial composite on the theory that the member companies represent alternative investment opportunities and that applicant must compete for funds with these firms in the money market. Although this evidence may be of some value from the standpoint of providing a broad overview, the Commission does not believe it appropriate to predicate a return recommendation on the experience of this large, diverse group, particularly without any detailed analysis of the characteristics of its members. The cornerstone of the alternative opportunity cost concept upon which the comparable earnings method is based is that the return authorized should be commensurate with returns being earned on investments in other business undertakings having similar or corresponding risks, but should not be so high as the returns which might be realized from highly profitable enterprises or speculative ventures. *Bluefield Waterworks Company v. Public Service Commission*, 262 U.S. 679 (1923). Thus, there must be a showing that the enterprises selected for comparative purposes are, in fact, comparable. There has been no such showing in this case, and the Commission can accord little weight to a return recommendation based on this data.

A comparable earnings approach was also employed by Mr. Jeffries in connection with his efforts to emphasize the importance of fixing a rate of return on common equity which will allow the company to attract capital on the most reasonable terms possible (App. Ex. 8, p. 24). Although applicant's bonds are still rated double-A by Moody's, they have been recently downgraded by Standard and Poor's to AA- (App. Ex. 8, p. 24). The company lost its double-A preferred stock rating in 1976 (App. Ex. 8, p. 28). As an improvement in the current ratings would result in lower financing costs to the company, the witness deemed it appropriate in recommending a rate of return on equity to evaluate the achieved return of electric utilities with double-A ratings for both preferred stock and bonds (App. Ex. 8, p. 43). This reduced the number in

the original group studied from sixteen to twelve. The resulting average return is slightly higher during the years since 1974 than the average return for the larger sample, with the exception of 1979 when it was actually lower. In no event, however, did this average return approach 15.0 percent, the lower bound of the witness' equity return recommendation. There is no need to repeat our earlier comments with respect to the inherent problems in the comparable earnings approach, but an additional observation is in order. There is much more involved in solidifying or improving applicant's present ratings than merely handing out rate increases, as company witness Maugans acknowledged (Tr. X, pp. 54-68; Tr. XII, pp. 164-166). Adequate rate relief is an important step, but utility management also has a definite role to play as it is the company's performance over time that influences the rating agencies. The Commission recognizes that improved ratings will lead to lower future financing costs, but the real question is what price we should ask the consumers to pay presently for this future benefit. This is the very heart of the rate of return inquiry, and a balance must be struck. Were it not for this consideration, we could simply send the rate of return witnesses home and decide the earnings requirement question solely through an analysis of coverage ratios. There is quite clearly more to establishing a reasonable earnings opportunity than a mechanical calculation designed to satisfy the rating agencies' coverage tests.

As a fourth measure of the appropriate return on common equity, Mr. Jeffries performed a risk premium analysis involving a comparison of the yield on new double-A rated utility bonds with the return on equity of double-A rated electrics for the years 1964 to 1978. The average equity-debt risk spread for the period was 5.91 percent (App. Ex. 8, p. 43). He then applied this risk spread to the average yield on newly issued bonds of similar rating for the twelve months ended August, 1979, which he calcu-

lated to be 9.6 percent (App. Ex. 8, p. 29). Summing the two numbers produced an indicated return on common equity of 15.51 percent. Staff witness Farrar, who also performed a risk premium analysis as a check on the reasonableness of his own cost of equity recommendation (S.R. 29, pp. 29-30), criticized Mr. Jeffries' use of achieved returns on common equity for purposes of establishing the annual differential (Staff Ex. 11, pp. 11-12). He argued that the use of achieved returns is improper as achieved returns do not necessarily reflect the actual cost of equity. The Commission notes that in the earlier years of the study, where the annual differential was the greatest, utility stocks were commonly sold above book value. This certainly lends support to Mr. Farrar's contention that the average risk spread employed by Mr. Jeffries is too high. However, even based on Mr. Jeffries' own method of calculation, we observe that the annual differential reached the average for the period only once in the 1970's and that was in 1972. If one limits the historical time frame of the analysis to what is clearly a more representative period in terms of future expectations, say 1975 through 1978, one gets far different results. Using Mr. Jeffries' numbers, the average equity-debt risk spread for the more recent period is 3.74 percentage points. Combining this risk premium with the 9.6 percent referred to above produces an indicated rate of return on common equity of 13.34 percent, a far cry from the 15.51 percent derived by Mr. Jeffries through his methodology but an extraordinarily good match with the 1979 data utilized in his comparable earnings test. Moreover, a risk differential of 3.74 percentage points exceeds that determined by Mr. Farrar who, it will be remembered, based his calculation on an estimate of the cost of equity rather than the realized return on equity. This effectively answers the charge that the risk premiums is understated during more recent years due to insufficient achieved returns (App. Ex. 8, p. 29).

Mr. Farrar had the benefit of final figures for calendar 1979 at the time he performed his original analysis (S.R., p. 30). At hearing, Mr. Jeffries updated his calculation of the average monthly yield on new double-A rated utility bonds to take into account the balance of the test year. His determination of the yield, 10.48 percent, exceeds slightly that calculated by Mr. Farrar as he limited his study to new issues. However, if we accept Mr. Jeffries number for the purpose at hand, and combine 10.48 percent with a risk premium of 3.74, the indicated return on common equity becomes 14.22 percent. Again, this is well below the witness's recommended range, but does fall well within the bounds of the staff witness's original recommendation.

The final method employed by Mr. Jeffries in arriving at his original recommended cost of equity was what he characterized as a "market based" approach (App. Ex. 8, pp. 22-23). Indeed, this is a version of the discounted cash flow analysis (DCF) familiar to the Commission and consistently approved by it in the past as an appropriate means of measuring investor expectations. Under his application of the method, Mr. Jeffries concluded that the base line cost of equity was 14.50 percent. He then adjusted this cost by 10 percent to recognize issuance costs, market pressure, and dilution (App. Ex. 8, p. 23). This produced a recommended return on equity of 15.95 percent.

Staff witness Farrar also based his cost of equity recommendation on a DCF analysis. As detailed in the staff report, he determined the base line cost of equity to be 13.58 percent (S.R., pp. 28-29). Applying the staff's customary adjustment factors of 1.032 and 1.10 to this base line costs resulted in an indicated cost of equity of from 14.01 to 14.94 percent.

Given our reservations with respect to the conclusions drawn by Mr. Jeffries from the other methods he employed, it is apparent that our decision as to the appropri-

ate return on equity comes down to a choice between Mr. Jeffries' and Mr. Farrar's DCF recommendations. Although applicant's witness Maugans also initially offered a cost of equity recommendation, his supplemental testimony relating to this area is largely devoted to a criticism of Mr. Farrar's analysis, and specifically accepts as fair the revised recommendation of Mr. Jeffries (App. Ex. 4A, p. 1). In light of this development, the Commission sees no purpose to be served by picking our way through Mr. Maugans' original proposal. We would note, however, that the testimony of Mr. Farrar raised significant questions as to the reasonableness of his methods (Staff Ex. 11, pp. 12-14).

Before considering the specifics of the competing positions of the applicant and the staff as to the proper application of the DCF formula for purposes of these proceedings, the Commission feels compelled to address certain charges contained in applicant's brief relative to the Commission's reliance on this method. Applicant apparently entertains the suspicion that the Commission's preference for the DCF approach is based on a belief that it is less subject to the vicissitudes of an individual witness's judgment than are other recognized methods (App. Brief, p. 36). This is simply not true. The Commission's general acceptance of DCF-based equity cost recommendations is grounded in the fact that DCF, by design, is a market measure of investor requirements, the very factor which must be isolated in determining the cost to the company of equity capital. The Commission has never intended to suggest that the application of the DCF formula is a mechanical process, as a review of our recent orders relative to this subject will bear out. (See, *e.g.*, *Cincinnati Gas and Electric Company*, Case No. 79-11-EL-AIR [January 7, 1980]; *Toledo Edison Company*, Case No. 79-143-EL-AIR [February 29, 1980]). Moreover, although the Commission has relied heavily on the DCF method in

the past, we have never intended to suggest that it is the only acceptable method for determining the cost of equity capital.

The DCF method is based on the premise that the cost of equity capital is equal to the sum of the current dividend yield and the rate of growth in dividends (S.R., pp. 47-50). Dividend yield is, of course, determined by dividing the common stock dividend by the price. Mr. Jeffries, who for purposes of his original testimony was limited to data available through August, 1979, calculated dividend yield to be 10.5 percent based on a dividend of $1.92 per share and an average market price of applicant's common stock of $18.25 for the then most recent twelve month period (App. Ex. 8, p. 22). Mr. Farrar, who had calendar 1979 data available at the time of his original study, determined the yield to be 11.33 percent based on a $2.00 dividend and a twelve-month average price of $17.65 (S.R., p. 29). Thus, the methods for determining yield were identical, both witnesses specifically agreeing that the use of a twelve-month average price was appropriate (App. Ex. 8, p. 22; Staff Ex. 11, p. 14). We will defer consideration of applicant's apparent change in position with respect to this component of the formula for our discussion of the revised recommendations of the witnesses.

The critical difference in the DCF methodology as applied by Mr. Jeffries and Mr. Farrar lies in their respective estimates of the proper value of the growth component of the formula. Mr. Jeffries estimated growth by computing annual growth rates for common stock book value, earnings per share, and dividends for the period 1968 through 1978: 4.7 percent, 3.2 percent, and 3.6 percent, respectively (App. Ex. 8, p. 41). He then assumed that earnings growth should receive less weighting than the other two elements when forming a judgment with respect to a future growth rate, and concluded that a 4.0

percent growth factor was reasonable (App. Ex. 8, p. 23). Mr. Farrar, on the other hand, estimated growth by use of the "b x r" approach, "b" equalling the retention rate of earnings, and "r", the earnings on the common equity funds retained (S.R., p. 29). Based on his review of the results of the "b x r" calculation for several different periods, his observations concerning the relationship between earnings and dividend growth, and the inferences he drew from the recent increase in yield of the company's common stock, he recommends a 2.25 per cent growth factor.

Applicant's witness Maugans was highly critical of Mr. Farrar's growth estimate, claiming his reliance on the "b x r" result for a two-year period represents a complete departure from the customary staff practice of analyzing at least five years data as a basis for this calculation (App. Ex. 4A, pp. 7-12). Mr. Maugans goes so far as to suggest that Mr. Farrar selected only the numbers he needed to produce an artificially low equity cost (App. Ex. 4A, p. 8). He points out that had Mr. Farrar used the method sponsored by the staff in the company's prior case (Case No. 78-677-EL-AIR), a growth rate of 3.73 percent would result (App. Ex. 4A, pp. 10-11). He also presented an exhibit depicting the growth component which would be produced by applying the method described in the staff reports issued in twelve other electric rate proceedings to Illuminating Company data (App. Ex. 4L). These fall generally in the area of 3.5 percent. The Commission believes that Mr. Maugans' criticisms are unwarranted, that his insinuations are improper, and that his comparisons are largely irrelevant.

It must be remembered that the "growth" element of the DCF formula is actually "expected growth" and, as such, is not susceptible to empirical measurement (S.R. p. 28; Tr. XXIV, p. 26). Thus, a witness must rely on judgment in making this growth determination, and different

witnesses may have legitimate differences of opinion as to what constitutes the best evidence upon which to base that judgment. Moreover, the same witness may quite properly reach a different conclusion as to what evidence represents the most reliable guide to future growth prospects in two different cases, based on the facts of each case. The Commission finds nothing untoward in the fact that Mr. Farrar chose to regard different data sets as more pertinent for purposes of his recommendation in these proceedings than those which other staff witnesses have drawn upon for growth estimates in other cases. The Commission readily concedes that the staff has never used less than a five year "b x r" for determining expected growth, although it is also evident from applicant's exhibit that the staff has, in fact, used a variety of different analyses in those cases cited (App. Ex. 4L). Mr. Farrar has fully described the basis for his growth estimate in this case, and his recommendation must stand or fall on its merits. It should not and will not be dismissed merely because it differs from staff conclusions in other cases.

The Commission must begin the review of Mr. Farrar's growth analysis by correcting applicant's repeated misstatement that the staff witness's estimate of growth is based only on a two-year "b x r" calculation (App. Ex. 4A, p. 7; Tr. XXIV, p. 20; App. Brief, p. 37). This is plainly not the fact. Mr. Farrar's analysis begins with his observation that the result of the "b x r" calculation for the year 1978 showed a precipitious drop from the "b x r" for prior years (Tr. XXIV, pp. 24-25). For the years 1978 and 1979, "b x r" was 1.84 percent and 2.48 percent, respectively, yielding an average "b x r" for this two-year period of 2.16 percent (Staff Ex. 11, p. 22). Mr. Farrar compared this figure to the "b x r" computed for the five-year period, 1975 through 1979, of 3.58 percent and the ten-year period, 1970 through 1979, of 3.77 percent (S.R., p. 29). The magnitude of the disparity prompted Mr. Farrar to explore

possible explanations for this break in the historic growth pattern. He noted that earnings per share for 1979 were well below the experience of 1974 (S.R., p. 29). As calculated by Mr. Farrar, the log-linear growth rate of earnings since 1974 was 0.76 percent (S.R., p. 29). For the period since 1975, it was 1.98 percent (S.R., p. 29). This evidence led Mr. Farrar to conclude that there may have been a basic restructuring between the yield and growth components of investor requirements relative to this utility (Staff Ex. 11, p. 9). This interpretation is certainly plausible in light of the decline in applicant's stock prices (Staff Ex. 11, p. 14). Growth expectations appear to have declined, while yield requirements have obviously increased. The use of a five-year average "b x r" would not be consistent with this explanation of the basis for the drastic change in "b x r" between 1977 and 1978. Based on the data discussed above, estimates of earnings growth from other sources (Tr. XXIV, p. 21), and historical earnings growth rates, both compound and log-linear (Tr. XXIV, p. 24), Mr. Farrar's opinion was that 2.25 percent represents a reasonable estimate of investor's future growth expectations.

Both of applicant's witnesses attempted to minimize the significance of earnings growth rates in determining the estimated growth in dividends for purposes of the DCF calculation (App. Ex. 8, p. 23; App. Ex. 4A, p. 11). It should be obvious, however, that a policy of continuing to increase dividends in the absence of corresponding increases in earnings can only be maintained for so long. As witness Maugans contends, applicant's dividend growth has been relatively stable for some time; but we have already seen that earnings growth has not kept pace (S.R., p. 29). This should in no way be taken as a criticism of applicant's dividend policy. It does, however, tend to support Mr. Farrar's position with respect to the import of the abrupt change in "b x r" in 1978. In 1978, applicant's divi-

dend payment ratio reached an all-time high (S.R., p. 32), and it was in 1978 that applicant's market-to-book ratio, on an annual basis, fell below 1.0 for the first time (S.R., p. 37). The Illuminating Company had historically been the strongest of the Ohio electrics in terms of market-to-book, but despite the fact that it had exhibited the most stable growth in dividends, and despite the fact that it was paying the second highest actual dividend of the other Ohio electrics, it entered 1978 with the poorest market-to-book ratio of the six companies (S.R., p. 33). Thus, as Mr. Farrar's analysis would suggest, it is certainly possible that by 1978 applicant's investors had come to recognize that the practice of increasing the current dividend without concomitant earnings support was nothing more than a borrowing from future dividends (Staff Ex 11, pp. 16-17). The historical dividend growth rate is certainly relevant in estimating future growth. However, earnings growth, and its relationship to dividends growth, is deserving of far more attention than either of applicant's witnesses devoted to it.

Having considered applicant's complaint that the period analyzed by Mr. Farrar for purpose of estimating the growth component of the DCF formula was too short, the Commission must, itself, question whether the period examined by Mr. Jeffries may not have been too long. It can be stated without fear of contradiction that the conditions faced by the electric utility industry today are vastly different from those which obtained prior to 1974. Indeed, Mr. Maugans expressly recognized this fact in limiting the risk permium analysis he described in his original testimony to the most recent five years (App. Ex. 4, p. 34). Upon cross-examination by staff counsel, he also agreed that in light of the changed circumstances it was unrealistic to expect the company to return to the earnings level of the period 1968 through 1977 (Tr. X, p. 38). Mr. Maugans listed a number of the more significant of these changed

conditions: unprecedented, sustained inflation; lower sales growth; increased fuel costs; more governmental and regulatory involvement in all aspects of operation; more consumer activism; increased lead times for the construction of generating facilities and the decrease in quality of earnings resulting from the attendant increase in AFUDC charges; and extremely volatile short and long-term interest rates (App. Ex. 4, pp. 34-35). Although it is readily apparent that these factors increase the risk to the equity investor and, accordingly, create much higher yield requirements, it is hard to understand why they should have any sort of sustaining effect on historical growth expectations.

In light of the foregoing discussion, the Commission is of the opinion that Mr. Farrar's estimate of expected growth is more reasonable than that offered by Mr. Jeffries. The 4.0 percent growth projection fails to adequately consider applicant's recent earnings history and is based on an analysis of a time period which includes years in which conditions were far different from those that may reasonably be anticipated in the future. Even if we were to assume the longer time frame to be appropriate, a mere change in the reference from 1968 through 1978, to 1970 through 1979, would produce a significant change in the earnings growth rate. Using the log-linear method, it drops from the 3.2 percent calculated by Mr. Jeffries to approximately 2.5 percent (Tr. XXIV, p. 24). The compound growth rate for the last ten years is just over 2.0 percent (Tr. XXIV, p. 24). Mr. Farrar's recommendation is internally consistent, for he couples his finding of investors' diminished future growth expectations with a recognition of their increased yield requirements. In fact, his recommended cost of equity is, to our knowledge, the highest ever sponsored by a staff witness and, at its upper bound, is certainly well above any heretofore authorized by the Commission. Further, the reasonableness of his 2.25 per-

cent growth rate is confirmed by the results of the risk premium analysis he performed which demonstrates that the use of a higher growth rate would have resulted in a risk differential far in excess of the average for the last five years (S.R., pp. 29-30). Applicant's objections relative to this area should be overruled.

The Commission's acceptance of a 2.25 percent growth component for the DCF calculation does not bring our rate of return inquiry to an end, as each of the witnesses significantly revised his original cost of equity recommendation at hearing. Mr. Jeffries summarized the changes in economic conditions which have occurred since the time his original testimony was filed (App. Ex. 8A, pp. 1-4). Among the most significant of these changes was the Federal Reserve Board's pronouncement of October 6, 1979, with respect to the adoption of a restrictive monetary policy designed to slow inflation. Indeed, the Commission has discussed the impact of this action in several recent rate orders. (See, *e.g., Cincinnati Gas and Electric Company,* Case No. 79-11-EL-AIR [January 7, 1980]; *Toledo Edison Company,* Case No. 79-143-EL-AIR [February 29, 1980]). As Mr. Jeffries observes, the prime rate was in the area of 13 percent in September of 1979. At the outset of the hearing in these matters it was in excess of 19 percent (App. Ex. 8A, p. 3). Mr. Maugans, in explaining the sensitivity of utility stock prices to prevailing interest rates, points out that on October 3, 1979, the price per share of applicant's common stock was $17.625, but by March 5, 1980, it had dropped to $14.25 (App. Ex. 4A, p. 4). Inflation has continued unabated (App. Ex. 8A, p. 3).

There is no doubt that the cost of equity capital to the company increased significantly during the period between October of 1979 and the time these matters came on for hearing at the beginning of April, 1980. The question is, however, how to appropriately recognize these

changes in the cost of capital analysis. It will be recalled that in their original testimony both Mr. Jeffries and Mr. Farrar based their determination of the DCF yield component on the average stock price for a twelve-month period. Both cautioned against the use of spot yields in the calculation. Consistent with that methodology, each of the witnesses updated their yield computations to include more recent market data. Mr. Jeffries used the average price for the twelve months ending with February, 1980 (App. Ex. 8A, p. 4). Mr. Farrar brought his calculation forward through March, 1980, which produced an even higher yield determination; specifically, 11.86 percent (Tr. XXIV, pp. 3-4). This update pushed Mr. Jeffries' original equity return recommendation to the 16.0 to 17.0 percent range (App. Ex. 8A, p. 4). Mr. Farrar's recommendation is now 14.56 to 15.52 percent. Yet despite the fact that Mr. Farrar used precisely the same method as its own witness, applicant now complains that staff's yield determination is unreasonable (App. Ex. 4A, pp. 6-7; App. Brief, p. 38).

Applicant argues that if the return authorized is to reflect current investor requirements, the yield component should be calculated with reference to the average stock price over the last quarter of 1979 and the first quarter of 1980 (App. Ex. 8A, p. 5). As precedent for such a measure, the company cites this Commission's decision in the *Cincinnati Gas and Electric Company* case, *supra*, wherein we did employ a three-month rather than a twelve-month period for determining price based on reasoning similar to that now espoused by the applicant. However, there are factors present here which persuade the Commission that the twelve-month period remains appropriate for purposes of these proceedings.

As indicated above, the period following the Federal Reserve Board's October, 1979, announcement saw a steady rise in the prime rate. In light of additional mone-

tary and credit actions taken by the Board in March of 1980 (App. Ex. 8A, p. 1), this trend was reinforced. At that time, no one could reasonably anticipate that this situation would reverse itself in the near-term, at least not to the degree that has actually been the case (Tr. X, p. 124). On April 21, 1980, the prime rate was 19¾ percent (Tr. X, p. 121), but by May 13, 1980, it had dropped to 16½ percent (Tr. XXVI, p. 73). Since the conclusion of the hearings in these matters, it has fallen to 12 percent (*Wall Street Journal*, June 13, 1980). As Mr. Maugans testified, the utility stock prices should tend to respond to a drop in interest rates somewhat more quickly than the market as a whole (Tr. X, p. 119). This prediction has proved accurate, as applicant's stock has rebounded from an all-time low to where it is now selling in the $17 to $18 per share range.

In light of these developments, Consumers' Counsel argues that the Commission should ignore, as extraordinary, the conditions which prompted the witnesses to revise their cost of equity recommendations (O.C.C. Brief, p. 11). The City of Cleveland advances a similar claim (City of Cleveland Brief, p. 8). Thus, on the one hand, we have the company contending that the data before October of 1979 is irrelevant, while on the other, we are confronted with intervenors' arguments that events since that time should not be considered. All this goes to point up the wisdom of Mr. Farrar's use of a twelve-month period for measuring yield in order to even out short-term fluctuations (Staff Ex. 11, p. 14). Under the circumstances of this case, the Commission believes Mr. Farrar's recommendation to be reasonable, and we accept his determination of the yield component as providing an appropriate basis for the DCF analysis.

Combining Mr. Farrar's yield of 11.86 percent with his estimate of expected growth of 2.25 percent produces a base line cost of equity 14.11 percent. After application

of the appropriate adjustment factors (S.R., p. 29), a range of 14.56 to 15.52 percent results. Although these limits have an aura of precision about them, it is clear from the foregoing discussion that the recommended range is no more than the summation of individual judgments. Given this fact, the Commission concludes that 15.0 percent, which falls at the approximate mid-point of this range, represents a reasonable estimate of the cost of equity capital to this utility.

Attrition Adjustment:

Applicant proposes an adjustment of some $13.8 million to account for inflation and to offset earnings erosion subsequent to the test period (App. Ex. 1, Sched. C-3.20, p. 103). The staff opposes the adjustment (S.R., pp. 17-18). Although presented as an expense adjustment, the Commission believes it appropriate to consider this item in connection with our rate of return discussion.

The Commission has had occasion to consider the question of an allowance for attrition in a number of its recent rate decisions. The specific proposals have taken a variety of forms ranging from an augmentation of the rate of return as presented by this company in its last rate case (*Cleveland Electric Illuminating Company,* Case No. 78-677-EL-AIR [May 2, 1979]), to adjustments to cost of service to reflect projected future expenses (See, *e.g., Dayton Power and Light Company,* Case No. 78-92-EL-AIR [March 9, 1979]). The Commission has generally rejected adjustments of this type, finding them to be inconsistent with the test-year concept of rate regulation (*Columbia Gas of Ohio, Inc.* [*Columbus*], Case No. 76-704-GA-AIR [June 29, 1977], aff'd *sub nom Franklin County Welfare Rights Organization v. Public Utilities Commission,* 55 Ohio St. 2d 1 [1978]). Although recognizing that regulated utilities are among the primary victims of inflation due to their inability to readily adjust prices, the Com-

mission has pointed out that reduced regulatory lag and appropriate expense annualizations have served to lessen its impact. More important, perhaps, from the standpoint of regulatory theory, is the fact that investors capitalize the risks of inflation in making their investment decisions. Thus, this element is reflected in the market price of the stock which, in turn, is built into the DCF analysis of the cost of equity upon which the authorized rate of return is based. The Supreme Court has recognized these considerations in upholding Commission decisions denying attrition allowances (*Franklin County Welfare Rights Organization v. Public Utilities Commission, supra; Masury Water Company v. Public Utilities Commission,* 58 Ohio St. 2d 1 [1979]).

Applicant correctly points out that the Commission has, in one prior instance, adjusted the allowed rate of return to recognize the impact of attrition on the resulting revenues (*Columbus and Southern Ohio Electric Company,* Case No. 78-1438-EL-AIR [December 29, 1979]). However, as the Commission was careful to explain in the order cited by applicant, that case involved a company facing a unique combination of circumstances which threatened its basic financial integrity. We do not believe that all those same factors have coalesced in this case. The Commission, therefore, rejects applicant's proposed attrition allowance for those reasons repeatedly stated in prior orders wherein we have considered this subject.

Rate of Return Summary:

Applying a cost of equity of 15.0 percent to the equity component of the capital structure approved herein produces, when combined with the findings relative to long-term debt and preferred stock, a weighted cost of capital of 10.82 percent. The Commission is of the opinion that a rate of return of 10.82 is sufficient to provide the company reasonable compensation for the electric service it renders customers affected by these proceedings.

AUTHORIZED INCREASE

A rate of return of 10.82 percent applied to the jurisdictional rate base of $1,485,734,000 approved for purposes of these proceedings results in an allowable return of $160,756,000. Certain expenses must be adjusted if the gross revenues authorized are to produce this dollar return. These adjustments, which have been calculated in a manner consistent with the findings herein, result in an increase in the allowance for federal income tax of $30,705,000, in the allowance for other taxes of $2,748,000, and in the provision for uncollectibles of $143,000. The net effect of these adjustments is to increase allowable expenses to $682,274,000. Adding the approved dollar return to the allowable expenses results in a finding that applicant is entitled to place rates in effect which will generate $843,030,000 in gross annual operating revenue. This represents an increase of $69,641,000 over the revenues which would be realized under applicant's present rate schedules. Similar calculations for the application area and the City of Cleveland would indicate that increases in gross annual revenues of $47,446,000 and $22,195,000 would be required if the applicant is to realize the dollar return resulting from the application of the authorized rate of return to the respective rate bases. Although our analysis suggests that the existing revenue deficiency is slightly greater in the City of Cleveland than in the application area, applicant has proposed a uniform increase in both rate areas. The Commission is of the opinion that the rates of return on the respective rate bases which result from maintaining uniform rates fall within acceptable limits around the jurisdictional rate of return and that rates may properly be established on a total jurisdiction basis.

Through filed objections to the staff report, several parties have taken exceptions to the staff's failure to address the question of whether the increase proposed by the company complies with guidelines promulgated by the Council

on Wage and Price Stability. The Commission has noted on a number of previous occasions that this agency is charged by statute to decide rate applications in accordance with state law and that the voluntary guidelines cannot limit the level of relief authorized (See, *e.g., Dayton Power and Light Company,* Case No. 78-92-EL-AIR [March 9, 1979]; *Dayton Power and Light Company,* Case No. 79-372-GA-AIR [May 7, 1980]). By its filing in these dockets of March 28, 1980, applicant presented an assessment of its compliance with the guidelines in which it indicates that even a grant of the full relief requested would not exceed the limitations. No other party presented evidence on the subject. The foregoing satisfies the Commission's reporting function.

The Commission is well aware of the fact that this company received rate relief a little over a year ago and that even as hearings were beginning in this case it filed notice of its intention to seek yet another rate increase. Inflation, of course, is the principal cause of applicant's ongoing financial dilemma, particularly with respect to its impact on costs associated with the company's construction program. Neither the company nor the Commission can control inflation, but, as discussed previously, there is reason to hope that the announced cancellation of four generating units will have some positive effects on applicant's financial outlook. There is, however, another area where even a modest improvement could have a significant impact with respect to the company's battle against earnings erosion.

The results of actual operations may be significantly influenced when some of a company's largest generating units exhibit poor equivalent availability. These are the very units which when operating at more reasonable capacity levels, produce the least expensive energy. Davis-Besse is obviously applicant's chief offender, a circumstance the Commission has recognized through the normal-

izing adjustment approved in the cost of service analysis in this case. However, there may be cost-effective improvements which could be pursued with respect to other of applicant's units as well. In its orders in *Columbus and Southern Ohio Electric Company,* Case No. 78-1438-EL-AIR (December 12, 1979) and *Cincinnati Gas and Electric Company,* Case No. 79-11-EL-AIR (January 7, 1980), the Commission described a staff program, undertaken in connection with the Department of Energy, to investigate the costs and benefits associated with improved power plant productivity. Staff witness Hunt offered testimony in these proceedings commending applicant for the steps taken to date to improve unit availability and urging that these efforts be continued (Staff Ex. 9, pp. 9-10). The staff recommends that the company be required to submit quarterly reports on the immediate past performance of its generating units, in a form to be agreed upon by the applicant and the staff, to be used in establishing a statewide power plant productivity data base to assist in monitoring power plant performance (Staff Ex. 9, pp. 10-11). In recognition of the importance the Commission attaches to this subject, we will so order.

TARIFFS

The recommendations offered by the staff after its review of applicant's proposed tariffs drew relatively few objections (S.R., pp. 52-61). Those staff recommendations not subject to specific objection or modification should be implemented. There are, however, several remaining tariff questions which the Commission must consider.

Customer Charge:

In applicant's last rate case, the Commission adopted a staff recommendation which introduced a customer charge component into applicant's residential and small commer-

cial rate schedules for the first time. This measure was consistent with all other recent electric rate orders. The purpose of the flat charge is to recognize that there are costs incurred by the company merely by virtue of the fact that a customer is on the system, without regard to usage considerations. Applicant's proposed residential tariffs include a customer charge of $3.00, a slight reduction from the $3.05 charge approved in the prior case. The staff considers the charge to be acceptable in light of the customer charges currently in effect for other utilities in the state (Staff Ex. 10, p. 3). Applicant's witness Bingham, who sponsored applicant's proposed tariffs, agreed with staff witness Groves that the concept of a customer charge was theoretically correct (App. Ex. 7A, p. 5). However, he noted that there had been poor customer acceptance of the charge as evidenced by the many complaints received by the company with respect thereto (App. Ex. 7A, p. 5). Customer acceptance is, of course, an important consideration in rate design, but it must be balanced against the also important principle that rates should reflect cost. Given the modest nature of the customer charge proposed and the fact that it actually represents a decrease from that currently in effect, the Commission believes this feature should be retained. It is hoped that customer opposition will diminish as experience is gained with the charge.

Energy Conservation Rate:

Applicant's proposed residential tariff continues the energy conservation schedule approved by the Commission in the company's prior rate case. This schedule is available to customers whose dwelling units meet certain insulation and other energy conservation standards. Intervenor City of Cleveland challenged this rate on the basis that it is not cost-justified, a fact which is somewhat ironic in that the Cleveland ordinance from which the complaint and appeal is taken also contains this rate provision. Based on

his analysis of a single study, City of Cleveland witness Rothey concluded that the rate was not cost-based (City of Cleveland Ex. 9, pp. 15-17). Cross-examination indicated that there was other relevant data which might have been considered (Tr. XXV, pp. 50-55), and the witness agreed that there were other considerations to be taken into account in rate designs in addition to cost of service principles (Tr. XXV, p. 49). No further discussion is required as the Supreme Court in *City of Cleveland v. Public Utilities Commission*, S. Ct. Case No. 79-1158 (July 9, 1978), 63 Ohio St. 2d (1980) reviewed this same schedule and determined that it furthered a proper objective. Intervenor's objection is overruled.

Space Heating and Water Heating Schedules:

Applicant's tariffs offer a separate rate for space heating and water heating customers whose appliances were installed prior to Commission orders closing the rate in *Cleveland Electric Illuminating Company*, Case No. 71-634-Y (November 28, 1979), Order on Remand (July 3, 1975). In reviewing the history of these provisions, the staff found that the original order closing the rate indicated that "customers" were to be grandfathered, while the language of applicant's tariffs limits the rate to "installations." The staff recommended that this language be amended to conform to the aforementioned orders. Applicant acknowledges that the orders in question do refer to "customers", but points out that the tariffs have always contained the "installation" phraseology. As these tariffs have been accepted for filing by a succession of Commission entries, Applicant argues that the Commission has approved the concept. We need not discuss the implications of these prior entries, for, no matter what they may have said, we now find that the availability of rate should be limited to existing customers. The idea advanced by applicant that some sort of property right attaches to the availability of this

rate is absurd (Tr. XVIII, pp. 28-29). There is no transferable property right in any utility rate. Although grandfathering may, on occasion, be appropriate for existing customers to give effect to equitable considerations, the very idea in closing a rate is that it will eventually disappear through attrition. How will this process proceed at any meaningful pace if the limiting provisions apply to installations rather than customers? Applicant's objection to the staff recommendation is overruled.

General Commercial Schedule:

Two questions exists with respect to the company's proposed general service schedule. Applicant proposed to reinstitute a two-part declining block rate in the summer rates contained in this schedule. The staff, although originally recommending rejection of the change, has now dropped its opposition. Applicant's witness Bingham amply supported the return to the two-block rate through his supplemental testimony (App. Ex. 7A, p. 4). This rate design is hereby approved for this schedule.

The second issue which has arisen with respect to this schedule is whether the return being earned from this service is inadequate when compared to the return on other services. Based on the cost of service study submitted in this case (App. Ex. 9, p. 1), applicant concluded that this was, in fact, the case. The staff concurs in this judgment (S.R., pp. 57-58). The Commission, therefore, directs that the proposed distribution of revenue requirements embodied in the rate schedules as originally filed be adjusted so that revenues under the general service schedule more nearly approximate the average return under the other schedules. In accordance with the recommendation of Mr. Bingham, the extent to which this change results in a lower revenue requirements from other customer classes should be recognized through a pro

rate reduction based on existing revenue levels (Tr. XVIII, pp. 27-28).

Effective Date:

The general practice of this Commission has been to fix the effective date of tariffs filed pursuant to its rate orders as thirty days following the issuance of the entry accepting the tariffs for filing. The purpose of this delay is to afford affected customers notice of the increase authorized through mailings by the company prior to the date the new rates become applicable. The Commission continues to believe this to be a reasonable practice, but finds circumstances present in this case which compel a departure from this policy.

Section 4909.42 Revised Code provides that if the Commission has not acted upon a rate increase application within 275 days of the date of filing, the applicant utility, upon the filing of an undertaking, may place its proposed rates into effect subject to the condition that amounts collected under rates charged which are in excess of those ultimately determined reasonable by the Commission must be refunded. The Commission makes every effort to issue its rate orders in advance of the expiration of 275-day time period in order to avoid the customer confusion which might result should the refund provision be invoked. Due to the extraordinary length of the hearings in these dockets, this was not possible in this instance. However, applicant has made no attempt to place its proposed rates in effect and the Commission believes that basic principles of fairness dictate that the company not be penalized for its forebearance. The Commission, therefore, finds the appropriate course in these proceedings to be to establish the effective date of the tariffs filed pursuant to this order as the date they are approved by Commission entry. The customer notification requirement will,

of course, be retained; said notice to be mailed to affected customers upon approval of its form by the Commission.

FINDINGS OF FACT:

From the evidence of record in these proceedings, the Commission now makes the following findings:

1) The value of all of applicant's property used and useful for the rendition of electric service to the customers affected by this application and complaint and appeal determined in accordance with Section 4909.05 and Section 4909.15 Revised Code as of the date certain of June 30, 1979, is not less than $1,485,734,000.

2) The value of the rate base properly allocable to the application area is not less than $1,030,866,000.

3) The value of the rate base properly allocable to the City of Cleveland is not less than $454,868,000.

4) For the twelve month period ending December 31, 1979, the test period in these proceedings, the revenues, expenses, and income available for fixed charges realized by applicant under its present permanent rate schedules were $773,389,000, $648,678,000, and $124,711,000, respectively.

5) The revenues, expenses, and income available for fixed charges realized by applicant in the application area were $542,489,000, $455,507,000, and $86,982,000, respectively.

6) The revenues, expenses, and income available for fixed charges realized by applicant the City of Cleveland under present rates now continued in effect by the ordinance complained of were $230,900,000, $193,171,000, and $37,729,000, respectively.

7) The total net annual compensation of $124,711,000 represents a rate of return of 8.39 percent on the jurisdictional rate base.

8) The net annual compensation of $86,982,000 realized by applicant in the application area represents a rate of return of 8.44 percent on the allocated rate base.

9) The net annual compensation of $37,729,000 realized by applicant in the City of Cleveland represents a rate of return of 8.29 percent on the allocated rate base.

10) Rates of return of 8.39 percent, 8.44 percent, and 8.29 percent are insufficient to provide applicant reasonable compensation for the electric service rendered customers affected by the application and complaint and appeal.

11) A rate of return of 10.82 percent is fair and reasonable under the circumstances presented by these cases and is sufficient to provide applicant just compensation and return on the value of its property used and useful in furnishing the service described in the application and complaint and appeal.

12) A rate of return of 10.82 percent applied to the the jurisdictional rate base of $1,485,734,000 will result in income available for fixed charges in the amount of $160,756,000.

13) The allowable annual expenses of applicant for purposes of these proceedings are $682,274,000.

14) The allowable gross annual revenue to which applicant is entitled for purposes of these proceedings is the sum of the amounts set forth in Findings 12 and 13, or $843,030,000.

15) Applicant's present tariffs should be withdrawn and cancelled and applicant should submit new tariffs consistent in all respects with the discussion and findings set forth above.

16) The tariffs submitted by applicant shall contain base (or non-fuel) rates and charges sufficient to yield gross revenues which will compensate the company for allowable test period operating expenses, exclusive of fuel costs includable in its fuel adjustment clause, and yield a 10.82 percent rate of return on its rate base of $1,485,734,000.

17) The provisions of these tariffs should be substituted for the provisions of Ordinance No. 1673-79 of the City of Cleveland.

18) Applicant shall be required to submit quarterly reports, in a form to be agreed upon by the company and the staff, detailing the immediate past performance of its generating units.

CONCLUSIONS OF LAW:

1) The application herein is filed pursuant to, and this Commission has jurisdiction thereof, under the provisions of Sections 4909.17, 4909.18 and 4909.19 Revised Code; further, applicant has complied with the requirements of the aforesaid statutes.

2) The instant complaint and appeal is filed pursuant to, and this Commission has jurisdiction thereof, under the provisions of Section 4909.34 Revised Code; further, applicant has complied with all applicable statutory requirements.

3) A staff investigation has been conducted and a report duly filed and mailed and public hearings have been held herein, the written notice thereof having complied with the requirements of Section 4909.19 Revised Code.

4) The existing rates and charges now being charged and collected by applicant for electric service to customers affected by this application are insufficient to provide the company with adequate net annual compensation and return

on its property used and useful in the rendition of electric service.

5) The rates for electric service contained in Ordinance No. 1673-79 of the City of Cleveland are insufficient to provide applicant adequate net annual compensation and return on its property used and useful in furnishing the service governed by said ordinance.

6) A rate of return of 10.82 percent is fair and reasonable under the circumstances of these cases and is sufficient to provide applicant just compensation and return on its property used and useful in the rendition of electric service to its customers.

7) Applicant should be authorized to cancel and withdraw its presently effective tariffs on file with this Commission and to file new tariffs consistent in all respects with the discussion and findings set forth above.

8) The provisions of these tariffs should be substituted for the provisions of Ordinance No. 1673-79 of the City of Cleveland.

ORDER:

It is, therefore,

ORDERED, That the application of Cleveland Electric Illuminating Company for authority to increase its rates and charges for electric service be, and hereby is granted to the extent provided in this Opinion and Order. It is, further,

ORDERED, That the complaint and appeal of Cleveland Electric Illuminating Company from Ordinance No. 1673-79 of the City of Cleveland be, and hereby is sustained and that relief be, and hereby is authorized to the extent provided in this Opinion and Order. It is, further,

ORDERED, That applicant be, and hereby is authorized to cancel and withdraw its present permanent tariffs and to file new tariffs consistent with the discussion and findings set forth above. Upon receipt of three (3) complete copies of tariffs conforming to this Opinion and Order, the Commission will review and approve same by entry. It is, further,

ORDERED, That the effective date of the new tariffs shall be the date said tariffs are accepted for filing. The new rates contained therein shall be applicable to all service rendered on or after the effective date. It is, further,

ORDERED, That applicant shall immediately commence notification of its customers of the increase in rates authorized herein by insert or attachment to its billings, by special mailing, or by a combination of these methods. Applicant shall submit a proposed form of notice to the Commission when it files its tariffs for approval and the Commission will review same and, if proper, approve it by entry. It is, further,

ORDERED, That applicant submit quarterly reports in a form to be agreed upon the company and the staff detailing the immediate past performance of its generating units. It is, further,

ORDERED, That all objections and motions not specifically discussed within this Opinion and Order or rendered moot thereby be, and hereby are overruled and denied. It is, further,

ORDERED, That copies of this Opinion and Order be served upon all parties of record.

D-92

THE PUBLIC UTILITIES
COMMISSION OF OHIO

/s/ WILLIAM S. NEWCOMB, JR.
(Chairman)

MICHAEL DELBANE
Voted no.

/s/ STEPHEN A. REILLY

(Commissioners)

Entered in the Journal

July 10, 1980

A True Copy

DAVID M. POLK

David M. Polk
Secretary

APPENDIX E

APPELLANT'S NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

(Filed September 2, 1981)

IN THE SUPREME COURT OF OHIO

OFFICE OF CONSUMERS' COUNSEL *Appellant* vs. THE PUBLIC UTILITIES COMMISSION OF OHIO *Appellee* and THE CLEVELAND ELECTRIC ILLUMINATING COMPANY *Intervening Appellee*	)	CASE NO. 80-1480
SENIOR CITIZENS COALITION, ET AL. *Appellant* vs. THE PUBLIC UTILITIES COMMISSION OF OHIO *Appellee* and THE CLEVELAND ELECTRIC ILLUMINATING COMPANY *Intervening Appellee*	)	CASE NO. 80-1528
CITY OF CLEVELAND *Appellant* vs. THE PUBLIC UTILITIES COMMISSION OF OHIO *Appellee* and THE CLEVELAND ELECTRIC ILLUMINATING COMPANY *Intervening Appellee*	)	CASE NO. 80-1547

APPEALS FROM THE PUBLIC UTILITIES COMMISSION OF OHIO
CASE NOS. 79-537-EL-AIR AND 79-774-EL-AIR

FILED
SEP - 2 1981
SUPREME COURT OF OHIO
THOMAS L. STARTZMAN, Clerk

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby taken that The Cleveland Electric Illuminating Company, intervening appellee before the Ohio Supreme Court, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of the State of Ohio entered in these proceedings on July 15, 1981, rehearing having been denied on September 1, 1981, which granted the appeals of the Office of Consumers' Counsel, the Senior Citizens Coalition, et al., and the City of Cleveland and reversed and remanded the July 10, 1980 Opinion and Order of The Public Utilities Commission of Ohio.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

Of Counsel:
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CRAIG I. SMITH, *Senior Counsel*
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(216) 687-8500
Counsel for The Cleveland Electric Illuminating Company

CERTIFICATE OF SERVICE

I hereby certify that true copies of the foregoing Notice of Appeal were served on all parties of record by mail to their last known addresses this 2nd day of September, 1981, as follows:

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APPENDIX F

OHIO STATUTES

OHIO REVISED CODE

§ 4905.02 "Public utility" defined.

As used in Chapter 4905. of the Revised Code, "public utility" includes every corporation, company, copartnership, person, or association, their lessees, trustees, or receivers, defined in section 4905.03 of the Revised Code, including all telephone companies, but excepting such other public utilities as operate their utilities not for profit, such other public utilities as are owned or operated by any municipal corporation, and railroads as defined in sections 4907.02 and 4907.03 of the Revised Code.

*HISTORY: 138 v H 21. Eff 7-2-80.

§ 4905.03 Definitions.

As used in Chapter 4905. of the Revised Code:

(A) Any person, firm, copartnership, voluntary association, joint-stock association, company, or corporation, wherever organized or incorporated, is:

(1) A telegraph company, when engaged in the business of transmitting telegraphic messages to, from, through, or in this state;

(2) A telephone company, when engaged in the business of transmitting telephonic messages to, from, through, or in this state and as such is a common carrier;

(3) A motor transportation company, when engaged in the business of carrying and transporting persons or property or the business of providing or furnishing such transportation service, for hire, in or by motor-propelled vehicles of any kind, including trailers, for the public in general, over any public street, road, or highway in this state, except as provided in section 4921.02 of the Revised Code;

(4) An electric light company, when engaged in the business of supplying electricity for light, heat, or power purposes to consumers within this state;

(5) A gas company, when engaged in the business of supplying artificial gas for lighting, power, or heating purposes to consumers within this state or when engaged in the business of supplying artificial gas to gas companies or to natural gas companies within this state, but a producer engaged in supplying to one or more gas or natural gas companies, only such artificial gas as is manufactured by such producer as a by-product of some other process in which such producer is primarily engaged within this state is not thereby a gas company. All rates, rentals, tolls, schedules, charges of any kind, or agreements between any gas company and any other gas company or any natural gas company providing for the supplying of artificial gas and for compensation for the same, are subject to the jurisdiction of the public utilities commission.

(6) A natural gas company, when engaged in the business of supplying natural gas for lighting, power, or heating purposes to consumers within this state, or when engaged in the business of supplying natural gas to gas companies or to natural gas companies within this state, but where a producer supplies to one or more gas or natural gas companies only such gas as is produced by such producer from wells drilled on land owned in fee by such producer or where the principal use of such land by said producer is other than the production of gas, within this state, such producer is not thereby a natural gas company. All rates, rentals, tolls, schedules, charges of any kind, or agreements between a natural gas company and other natural gas companies or gas companies providing for the supply of natural gas and for compensation for the same, are subject to the jurisdiction of the public utilities commission. The commission may, upon application made to it, relieve any producer of natural gas, defined in this

section as a gas company or a natural gas company of compliance with the obligations imposed by Chapters 4901., 4903., 4905., 4907., 4909., 4921., and 4923. of the Revised Code, so long as such producer is not affiliated with or under the control of a gas company or a natural gas company engaged in the transportation or distribution of natural gas, or so long as such producer does not engage in the distribution of natural gas to consumers.

(7) A pipe-line company, when engaged in the business of transporting natural gas, oil, or coal or its derivatives through pipes or tubing, either wholly or partly within this state;

(8) A water-works company, when engaged in the business of supplying water through pipes or tubing, or in a similar manner, to consumers within this state;

(9) A heating or cooling company, when engaged in the business of supplying water, steam, or air through pipes or tubing to consumers within this state for heating or cooling purposes;

(10) A messenger company, when engaged in the business of supplying messengers for any purpose;

(11) A street railway company, when engaged in the business of operating as a common carrier, a railway, wholly or partly within this state, with one or more tracks upon, along, above or below any public road, street, alleyway, or ground, within any municipal corporation, operated by any motive power other than steam and not a part of an interurban railroad, whether such railway is termed street, inclined-plane, elevated, or underground railway;

(12) A suburban railroad company, when engaged in the business of operating as a common carrier, whether wholly or partially within this state, a part of a street railway constructed or extended beyond the limits of a municipal corporation, and not a part of an interurban railroad;

(13) An interurban railroad company, when engaged in the business of operating a railroad, wholly or partially within this state, with one or more tracks from one municipal corporation or point in this state to another municipal corporation or point in this state, whether constructed upon the public highways or upon private rights of way, outside of municipal corporations, using electricity or other motive power than steam power for the transportation of passengers, packages, express matter, United States mail, baggage, and freight. Such interurban railroad company is included in the term "railroad" as used in section 4907.02 of the Revised Code;

(14) A sewage disposal system company, when engaged in the business of sewage disposal services through pipes or tubing, and treatment works, or in a similar manner, within this state.

(B) "Motor-propelled vehicle" means any automobile, automobile truck, motor bus, or any other self-propelled vehicle not operated or driven upon fixed rails or tracks.

Nothing in this section shall be construed to mean that an electric light company operated not for profit or one that is owned or operated by a municipal corporation is subject to sections 4905.66, 4905.67, 4905.68, and 4905.69 of the Revised Code.

*HISTORY: 138 v H 21. Eff 7-2-80.

§ 4905.04 Power to regulate public utilities and railroads.

The public utilities commission is hereby vested with the power and jurisdiction to supervise and regulate public utilities and railroads, to require all public utilities to furnish their products and render all services exacted by the commission or by law, and to promulgate and enforce all orders relating to the protection, welfare, and safety of railroad employees and the traveling public, including the apportionment between railroads and the state and its

political subdivisions of the cost of constructing protective devices at railroad grade crossings.

HISTORY: GC § 614-3; 102 v 549, § 5; 113 v 256; 129 v 313. Eff 9-21-61.

§ 4905.05 Scope of jurisdiction. (GC § 614-4)

The jurisdiction, supervision, powers, and duties of the public utilities commission extend to every public utility and railroad, the plant or property of which lies wholly within this state and when the property of a public utility or railroad lies partly within and partly without this state to that part of such plant or property which lies within this state, and to the persons or companies owning leasing, or operating such public utilities and railroads, and to the records and accounts of the business thereof within this state.

HISTORY: GC § 614-4; 102 v 549(552), § 6. Eff 10-1-53.

§ 4905.06 General supervision.

The public utilities commission shall have general supervision over all public utilities within its jurisdiction as defined in section 4905.05 of the Revised Code, and shall have power to examine such public utilities and keep informed as to their general condition, capitalization, and franchises, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, the safety and security of the public and their employees, and their compliance with all laws, orders of the commission, franchises, and charter requirements. The commission, through the public utilities commissioners or inspectors or employees of the commission authorized by it, may enter in or upon, for purposes of inspection, any property, equipment, building, plant, factory, office, apparatus, machinery, device, and lines of any public utility. The public utilities commission shall inspect, for the pur-

poses of the public safety, all gas and natural gas pipelines owned, operated, or controlled by public utilities as defined by sections 4905.02 and 4905.03 of the Revised Code, by municipalities, or by utilities operated not for profit. The power to inspect shall include the power to prescribe any rule or order that the public utilities commission finds necessary for protection of the public safety.

HISTORY: GC § 614-8; 102 v 549, § 10 (Eff 10-1-53); 136 v H 1297. Eff 1-11-77.

§ 4909.15 Fixation of reasonable rate.

(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:

(1) The valuation as of the date certain of the property of the public utility used and useful in rendering the public utility service for which rates are to be fixed and determined. The valuation so determined shall be the total value as set forth in division (J) of section 4909.05 of the Revised Code, and a reasonable allowance for materials and supplies and cash working capital, as determined by the public utilities commission. The commission may, in its discretion, permit a reasonable allowance for construction work in progress but, in no event, may any allowance for construction work in progress be made by the commission until it has determined, after a physical inspection, that the particular construction project is at least seventy-five percent complete.

(2) A fair and reasonable rate of return to the utility on the valuation as determined in division (A)(1) of this section;

(3) The dollar annual return to which the utility is entitled by applying the fair and reasonable rate of return as determined under division (A)(2) of this section to the valuation of the utility determined under division (A)(1) of this section;

(4) The cost to the utility of rendering the public utility service for the test period less the total of any interest on cash or credit refunds paid, pursuant to section 4909.42 of the Revised Code, by the utility during the test period. Federal, state, and local taxes imposed on or measured by net income may, in the discretion of the commission, be computed by the normalization method of accounting, provided the utility maintains accounting reserves that reflect differences between taxes actually payable and taxes on a normalized basis, provided that no determination as to the treatment in the rate making process of such taxes shall be made that will result in loss of any tax depreciation or other tax benefit to which the utility would otherwise be entitled, and further provided that such tax benefit as redounds to the utility as a result of such a computation may not be retained by the company, used to fund any dividend, or utilized for any purpose other than the defrayal of the operating expenses of the utility and the defrayal of the expenses of the utility in connection with construction work.

(B) The public utilities commission shall compute the gross annual revenues to which the utility is entitled by adding the dollar amount of return under division (A)(3) of this section to the cost of rendering the public utility service for the test period under division (A)(4) of this section.

(C) The test period, unless otherwise ordered by the public utilities commission, shall be the twelve-month period beginning six months prior to the date the application is filed and ending six months subsequent to that date. The revenues and expenses of the utility shall be determined during the test period. The date certain shall be not later than the date of filing.

(D) When the public utilities commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section, that any rate,

fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is, or will be, unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law, that the service is, or will be, inadequate, or that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

(1) With due regard among other things, to the value of all property of the public utility actually used and useful for the convenience of the public as determined under division (A)(1) of this section, excluding from such value the value of any franchise or right to own, operate, or enjoy the same in excess of the amount, exclusive of any tax or annual charge, actually paid to any political subdivision of the state or county, as the consideration for the grant of such franchise or right, and excluding any value added to such property by reason of a monopoly or merger, with due regard in determining the dollar annual return under division (A)(3) of this section to the necessity of making reservation out of the income for surplus, depreciation, and contingencies, and;

(2) With due regard to all such other matters as are proper, according to the facts in each case,

(a) Including a fair and reasonable rate of return determined by the commission with reference to a cost of debt equal to the actual embedded cost of debt of such public utility,

(b) But not including the portion of any periodic rental or use payments, representing that cost of property which is included in the valuation report under divisions (F) and (G) of section 4909.05 of the Revised Code, fix and determine the just and reasonable rate, fare, charge,

toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one. After such determination and order no change in the rate, fare, toll, charge, rental, schedule, classification, or service, shall be made, rendered, charged, demanded, exacted, or changed by such utility without the order of the commission, and any other rate, fare, toll, charge, rental, classification, or service is prohibited.

(E) Upon application of any person or any public utility, and after notice to the parties in interest and opportunity to be heard as provided in Chapters 4901., 4903., 4905., 4907., 4909., 4921., and 4923. of the Revised Code for other hearings, has been given, the commission may rescind, alter, or amend an order fixing any rate, fare, toll, charge, rental, classification, or service, or any other order made by the commission. Certified copies of such orders shall be served and take effect as provided for original orders.

In no event shall an allowance for construction work in progress under division (A)(1) of this section exceed twenty percent of the total valuation as stated in such division not including such allowance.

*HISTORY: 137 v H 230 (Eff 10-9-77); 138 v H 657 (Eff 9-24-79); 138 v H 736. Eff 10-16-80.

§ 4909.18 Application.

Any public utility desiring to establish any rate, joint rate, toll, classification, charge, or rental, or to modify, amend, change, increase, or reduce any existing rate, joint rate, toll, classification, charge, or rental, or any regulation or practice affecting the same, shall file a written application with the public utilities commission. Such application

shall be verified by the president or a vice-president and the secretary or treasurer of the applicant. Such application shall contain a schedule of the existing rate, joint rate, toll, classification, charge, or rental, or regulation or practice affecting the same, a schedule of the modification amendment, change, increase, or reduction sought to be established, and a statement of the facts and grounds upon which such application is based. If such application proposes a new service or the use of new equipment, or proposes the establishment or amendment of a regulation, the application shall fully describe the new service or equipment, or the regulation proposed to be established or amended, and shall explain how the proposed service or equipment differs from services or equipment presently offered or in use, or how the regulation proposed to be established or amended differs from regulations presently in effect. The application shall provide such additional information as the commission may require in its discretion. If the commission determines that such application is not for an increase in any rate, joint rate, toll, classification, charge, or rental, the commission may permit the filing of the schedule proposed in the application and fix the time when such schedule shall take effect. If it appears to the commission that the proposals in the application may be unjust or unreasonable, the commission shall set the matter for hearing and shall give notice of such hearing by sending written notice of the date set for the hearing to the public utility and publishing notice of the hearing one time in a newspaper of general circulation in each county in the service area affected by the application. At such hearing, the burden of proof to show that the proposals in the application are just and reasonable shall be upon the public utility. After such hearing, the commission shall, where practicable, issue an appropriate order within six months from the date the application was filed.

If the commission determines that such application is for an increase in any rate, joint rate, toll, classification,

charge, or rental there shall also, unless otherwise ordered by the commission, be filed with the application in duplicate the following exhibits:

(A) A report of its property used and useful in rendering the service referred to in such application, as provided in section 4909.05 of the Revised Code;

(B) A complete operating statement of its last fiscal year, showing in detail all its receipts, revenues, and incomes from all sources, all of its operating costs and other expenditures, and any analysis such public utility deems applicable to the matter referred to in said application;

(C) A statement of the income and expense anticipated under the application filed;

(D) A statement of financial condition summarizing assets, liabilities, and net worth;

(E) A proposed notice for newspaper publication fully disclosing the substance of the application. The notice shall prominently state that any person, firm, corporation, or association may file, pursuant to section 4909.19 of the Revised Code, an objection to such increase which may allege that such application contains proposals that are unjust and discriminatory or unreasonable. The notice shall further include the average percentage increase in rate that a representative industrial, commercial, and residential customer will bear should the increase be granted in full;

(F) Such other information as the commission may require in its discretion.

HISTORY: GC § 614-20; 102 v 549, § 22; 108 v Pt II 1094; 110 v 366; 113 v 16; 119 v 275; 136 v S 94. Eff 9-1-76.

§ 4909.19 Publication; investigation.

Upon the filing of any application for increase provided for by section 4909.18 of the Revised Code the public utility shall forthwith publish the substance and prayer of such application, in a form approved by the

public utilities commission, once a week for three consecutive weeks in a newspaper published and in general circulation throughout the territory in which such public utility operates and affected by the matters referred to in said application, and the commission shall at once cause an investigation to be made of the facts set forth in said application and the exhibits attached thereto, and of the matters connected therewith. Within a reasonable time as determined by the commission after the filing of such application, a written report shall be made and filed with the commission, a copy of which shall be sent by registered mail to the applicant, the mayor of any municipal corporation affected by the application, and to such other persons as the commission deems interested. If no objection to such report is made by any party interested within thirty days after such filing and the mailing of copies thereof, the commission shall fix a date within ten days for the final hearing upon said application, giving notice thereof to all parties interested. At such hearing the commission shall consider the matters set forth in said application and make such order respecting the prayer thereof as to it seems just and reasonable.

If objections are filed with the commission within thirty days after the filing of such report, the application shall be promptly set down for hearing of testimony before the commission or be forthwith referred to an attorney examiner designated by the commission to take all the testimony with respect to the application and objections which may be offered by any interested party. The commission shall also fix the time and place to take testimony giving ten days' written notice of such time and place to all parties. The taking of testimony shall commence on the date fixed in said notice and shall continue from day to day until completed. The attorney examiner may, upon good cause shown, grant continuances for not more than three days, excluding Saturdays, Sundays, and holidays. The

commission may grant continuances for a longer period than three days upon its order for good cause shown. At any hearing involving rates or charges sought to be increased, the burden of proof to show that the increased rates or charges are just and reasonable shall be on the public utility.

When the taking of testimony is completed, a full and complete record of such testimony noting all objections made and exceptions taken by any party or counsel, shall be made, signed by the attorney examiner, and filed with the commission. Thereafter, the commission shall make such order respecting the prayer of such application as seems just and reasonable to it.

In all proceedings before the commission in which the taking of testimony is required, except when heard by the commission, attorney examiners shall be assigned by the commission to take such testimony and fix the time and place therefor, and such testimony shall be taken in the manner prescribed in this section. All testimony shall be under oath or affirmation and taken down and transcribed by a reporter and made a part of the record in the case. The commission may hear the testimony or any part thereof in any case without having the same referred to an attorney examiner and may take additional testimony. Testimony shall be taken and a record made in accordance with such general rules as the commission prescribes and subject to such special instructions in any proceedings as it, by order, directs.

HISTORY: GC § 614-20; 102 v 549, § 22; 108 v Pt II 1094; 110 v 366; 113 v 16; 119 v 275; 136 v S 94. Eff 9-1-76.

§ 4905.22 Service and facilities required; unreasonable charge prohibited. (GC §§ 614-12, 614-13)

Every public utility shall furnish necessary and adequate service and facilities, and every public utility shall

furnish and provide with respect to its business such instrumentalities and facilities, as are adequate and in all respects just and reasonable. All charges made or demanded for any service rendered, or to be rendered, shall be just, reasonable, and not more than the charges allowed by law or by order of the public utilities commission, and no unjust or unreasonable charge shall be made or demanded for, or in connection with, any service, or in excess of that allowed by law or by order of the commission.

HISTORY: GC §§ 614-12, 614-13; 102 v 549(553), § 14; 102 v 549(554), § 15. Eff 10-1-53.

§ 4909.43 [Rate increase application filing date.]

(A) No public utility shall file a rate increase application covering a municipal corporation pursuant to section 4909.18 or 4909.35 of the Revised Code at any time prior to six months before the expiration of an ordinance of that municipal corporation enacted for the purpose of establishing the rates of that public utility.

(B) Not later than ninety days prior to the filing of an application pursuant to section 4909.18 or 4909.35 of the Revised Code, a public utility shall notify, in writing, the mayor and legislative authority of each municipality included in such application of the intent of the public utility to file an application, and of the proposed rates to be contained therein.

HISTORY: 136 v S 94. Eff 9-1-76.

OHIO ADMINISTRATIVE CODE

§ 4901:1-9-05 Uniform classification of accounts for electric utilities: FPC, 1961

The system of accounts and records, identified and designated as "Uniform System of Accounts Prescribed for Public Utilities and Licensees, effective January 1,

1961," as adopted by the Federal Power Commission, is adopted by this Commission effective as of January 1, 1961, for electric light companies operating within the State of Ohio which are subject to the jurisdiction of the Federal Power Commission except to the extent that the provisions of said Uniform System of Accounts are inconsistent in any way with the outstanding orders of this Commission pertaining to the accounting treatment to be followed with respect to emergency facilities and the Federal income tax results thereof and with respect to accelerated depreciation and the Federal income tax results thereof. This Commission reserves to itself the right to require the creation and maintenance of such additional accounts as may hereafter be prescribed, to cover the accounting procedure of such electric light companies operating in the State of Ohio. Each such public utility shall carry on its books, in addition to such additional accounts as may hereafter be prescribed by this Commission, the accounts and records prescribed in said Uniform System of Accounts effective January 1, 1961, for a public utility of its class, and shall accordingly keep such accounts in accordance with the requirements, definitions and instructions contained and set forth in said uniform system of accounts except to the extent that the provisions of said Uniform System of Accounts are inconsistent in any way with the outstanding orders of this Commission pertaining to the accounting treatment to be followed with respect to emergency facilities and the Federal income tax results thereof and with respect to accelerated depreciation and the Federal income tax results thereof in the stead and in lieu of the accounts and records prescribed by the provisions of rule 4901:1-9-02.

HISTORY: Eff. 1-20-63
Former Rule 25.05

OHIO SUPREME COURT RULES

Rule IX

MOTIONS FOR REHEARING AND ISSUANCE OF MANDATE

Section 1. Motion for Rehearing

A motion for rehearing shall be filed within ten days after the announcement of the decision. Such motion must be confined strictly to the grounds urged for rehearing and must not constitute a reargument of the case. Notice of such motion shall be served on opposing counsel who shall have five days to file his memorandum contra.

Section 2. Issuance of Mandate

Ten days after the announcement of a decision on the merits, unless a motion for rehiring is filed, the Clerk shall issue a mandate in conformity to the entry of the Court. If a motion for rehearing is filed and denied, the mandate shall issue at the same time as the decision on the motion for rehearing. No mandate shall issue on denial of a motion to certify or a motion for leave to appeal, or upon the sustaining of a motion to dismiss an appeal as one not involving a substantial constitutional question.

Motion to Dismiss or Affirm

1

Office - Supreme Court, U.S.
FILED
JAN 4 1982
ALEXANDER L. STEVAS,
CLERK

CASE No. 81-1002

In The

SUPREME COURT OF THE UNITED STATES

October Term, 1981

The Cleveland Electric Illuminating Company,
Appellant,

vs.

Office of the Consumers' Counsel
Senior Citizens Coalition, et al.
City of Cleveland

and

The Public Utilities Commission of Ohio,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF OHIO

MOTION OF APPELLEE, CITY OF CLEVELAND, TO DISMISS APPEAL

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QUESTIONS PRESENTED

1. Whether this Court lacks jurisdiction because the issues now presented to this Court were not timely raised in the Court below.

2. Whether this Court lacks jurisdiction because Appellant has failed to allege any statutory deprivation of a constitutionally protected right or property.

3. Whether the interpretation and application of purely State statutory law by a State Supreme Court is reviewable by this Court.

TABLE OF CONTENTS

	Page
Questions Presented	i
Table of Authorities	iv
Statement of the Case	1
Statement of Facts	6
Argument	12
A. THIS COURT LACKS JURISDICTION BECAUSE APPELLANT FAILED TO TIMELY RAISE ITS ALLEGED CONSTITUTIONAL QUESTIONS IN THE COURT BELOW.	
1. CEI Did Not Raise Any Constitutional Claims In Its Initial Brief Or Oral Argument Before The Ohio Supreme Court.	
2. CEI Cannot Claim "Surprise" By The Holding of the Ohio Supreme Court, And Was Not, Therefore, Entitled To Raise The Federal Question On Motion For Rehearing To That Court.	18
B. THIS COURT LACKS JURISDICTION BECAUSE APPELLANT HAS FAILED TO RAISE ANY CONSTITUTIONAL ISSUE.	21

Page

C. APPELLANT'S CLAIMS INVOLVE MATTERS OF PURELY LOCAL INTEREST. 28

Conclusion 31

Appendix

Ohio Statutes:

Ohio Revised Code Sections:
4903.10 A-1
4909.16 A-4

Ohio Supreme Court Rule of Procedure V A-5

TABLE OF AUTHORITIES

Page

CASES

Beck v. State of Washington, 369 U.S. 541 (1962) 13

Bluefield Waterworks v. Public Service Commission, 262 U.S. 679 (1923) 22, 24, 30

Charleston Federal Savings & Loan Association v. Alderson, 324 U.S. 182 (1944) 12

Cincinnati v. Cameron, 33 Ohio St. 336 (1878) . 11

City of Cleveland v. Public Utilities Commission, 63 Ohio St 2d 62, 406 N.E. 2d 1370 (1980) . . 10

Columbus and Southern Ohio Electric Co. v. Public Utilities Commission, 64 Ohio St. 2d 175, 413 N.E. 2d 1208 (1980) cert. denied, _ U.S. _, 101 S. Ct. 2071 (1981) . 10, 19

Consumers' Counsel v. Public Utilities Commission, 67 Ohio St. 2d 372, 424 N.E. 2d 300 (1981) 8

Page

Consumers' Counsel, et al. v. Public Utilities Commission, 67 Ohio St. 2d 153, 423 N.E. 2d 820 (1981) 6, 8, 9, 20, 23, 26, 29

Consumers' Counsel v. Public Utilities Commission, 58 Ohio St. 2d 449, 391 N.E. 2d 311 (1979). 10, 19

Dewey v. Des Moines, 173 U.S. 193 (1899) . . . 13, 16

Drake v. Bucher, 5 Ohio St. 2d 37, 213 N.E. 2d 182 (1966) 14

East Ohio Gas Co. v. Public Utilities Commission, 133 Ohio St. 212, 12 N.E. 2d 765 (1938). 19

Federal Power Commission v. The Natural Gas Co., 320 U.S. 591 (1944) . . . 17, 21, 24, 25

New York, ex rel. Bryant v. Zimmerman, 278 U.S. 63 (1928) 13, 17

Pruneyard Shopping Center v. Robbins, 447 U.S. 74 (1980) 18

Page

Re Arizona Public Service Co., Decision No. 51009 (Arizona Corp. Comm. 1980) 28

Re Northern States Power Co., Case No. 10049 (Pub. Serv. Comm. of N.D. 1980) 28

Washington Gas & Light Co. v. Baker, 188 F. 2d 11 (D.C. Cir. 1950), cert. denied 340 U.S. 952 (1951) . . . 24

STATUTES

Ohio Revised Code Title 49 . . 23
Ohio Revised Code Section 4903.10 2
Ohio Revised Code Section 4909.15 . . . . . 3, 8, 9, 29
Ohio Revised Code Section 4909.16 25
Ohio Revised Code Section 4909.18 1

RULES

Ohio Supreme Court Rule of Practice V 13
Ohio Supreme Court Rule of Practice IX 3
United States Supreme Court Rule of Practice 15 5

Page

TEXTS

5 Ohio Jurisprudence 3d,
Appellate Review
Sec. 510 (1978) 11

I. STATEMENT OF THE CASE

On September 17, 1979, Cleveland Electric Illuminating Company ("CEI") filed an application for a $79.8 million increase in rates with the Public Utilities Commission of Ohio ("Commission") pursuant to Ohio Revised Code Section 4909.18. Said application sought approval of rates which would yield approximately a fifteen percent (15%) increase in rates based on a 1979 test year. Said application did not include a request for reimbursement for the planning costs for four planned but never built nuclear power plants which is the subject of the within appeal. Approximately four and one-half months after the original request was filed, CEI amended its application to include, inter alia, a request for an out-of-test-year amortization of these planning

costs at $6.5 million per year.

On July 10, 1980, the Commission issued its Opinion and Order authorizing CEI to increase its rates and charges for electric service by $69,600,000 per year. Included within this amount was the requested $6.5 million amortization of the planning and design costs of the unbuilt power plants over ten (10) years. The Commission's Order establishing these rates, including the subject expense adjustment, went into effect on July 10, 1980. Timely Applications for Rehearing filed by all parties to the Commission proceedings, pursuant to Section 4903.10 Revised Code, were denied by the Commission on September 3, 1980. On November 3, 1980, the City of Cleveland, the Senior Citizens' Coalition and the Office of Consumers' Counsel (Appellees herein), filed Notices of Appeal to the Supreme Court of Ohio. On July 15, 1981

the Supreme Court of Ohio held that the Commission had exceeded its statutory authority in allowing the expenses related to the unbuilt power plants since these costs were not related to providing utility service to the consumer during the test period and, therefore, did not qualify for inclusion under Ohio's statutory ratemaking law, specifically Ohio Revised Code Section 4909.15.

On July 24, 1981, CEI filed a Motion for Rehearing with the Ohio Supreme Court. The effect of this motion was to stay issuance of the Court's mandate to the Public Utilities Commission to lower CEI's rates by the $6.5 million per year the Court had found illegal. Ohio Supreme Court Rule IX(2). The Ohio Supreme Court denied CEI's Motion for Rehearing on September 1, 1981. Notice of Appeal to this Court was filed with the Ohio Supreme Court on September 2, 1981.

Upon motion of the City of Cleveland and the Ohio Consumers' Counsel, the Commission initiated a proceeding requiring CEI to show cause why its rates should not be reduced in accordance with the Ohio Supreme Court's mandate. On September 22, 1981, CEI filed an Application for Stay of Execution and Enforcement of the Judgment of the Supreme Court of Ohio. On September 24, 1981, the Honorable Justice Byron White contacted the parties requesting that the parties brief the question as to whether Appellant CEI had timely raised its alleged constitutional issues before the Ohio Supreme Court. A brief on this subject was filed by CEI on September 29, 1981 with a Joint Brief in Opposition filed on behalf of the three Appellees, Office of Consumers' Counsel, City of Cleveland and Senior Citizens' Coalition, et al., on September 28, 1981. On October 2, 1981, the City of

Cleveland filed a Brief in Opposition to Appellant's Application for Stay. Briefs in Opposition were subsequently filed by the Office of Consumers' Counsel and the Senior Citizens' Coalition, et al. On October 12, 1981, this Court entered the following Order:

> "The application for stay of execution and enforcement of the judgment of the Supreme Court of Ohio presented to Justice White and by him referred to the Court is denied."

On November 25, 1981, Appellant filed its jurisdictional statement to which this Motion for Dismissal is addressed.[1]

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[1] CEI's jurisdictional statement is defective in that it fails to name the Appellee City of Cleveland, Ohio. Dismissal is warranted under the Rules of the Supreme Court of the United States, Rule 15(1)(b).

II. STATEMENT OF FACTS

The case below which gives rise to the present appeal involved an application to the Commission by the Appellant CEI to recover the planning costs of four (4) power plants which were never built. The plans were abandoned on January 23, 1980. The record below is replete with factual disputes as to whether CEI's continued expenditures for these plants were prudent, in light of steadily decreasing demand for electric service in the Cleveland, Ohio area. Although the Commission found that the costs related to the plants were prudently incurred, the Ohio Supreme Court rejected the Commission's prudency test and, therefore, did not reach the City of Cleveland's assignment of error challenging the Commission's finding on that point. Consumers' Counsel, et al. v.

Public Utilities Commission, 67 Ohio St.2d 153, 163, 168, 423 N.E.2d 820, 826, 829 (1981). There was no dispute that the plants were never built and thus never used to provide service to CEI's customers. The date on which CEI cancelled the plants in question, January 23, 1980, was clearly beyond the 1979 test year at issue in the proceedings below.

In their respective appeals to the Supreme Court of Ohio, the City of Cleveland, the Office of Consumers' Counsel and the Senior Citizens' Coalition, et al. argued, inter alia, that the Commission had exceeded its statutory authority when it allowed the expenses for the planned, but unbuilt, power plants because the expenses were not related to property used and useful in rendering electric

service during the test year.[2]

Both CEI and the Commission limited their arguments in brief and oral argument before the Court to issues of Ohio statutory law. No mention was made by CEI in its initial brief or oral argument before the Court of the alleged constitutional issues it now raises before this Court.

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[2] The City of Cleveland challenged the Commission's ruling on the additional ground that the expense was incurred beyond the 1979 test year. Ohio Revised Code Section 4909.15(c) provides that rates can be based only upon expenses incurred during the test year and related to property used to render the utility service. See Office of Consumers' Counsel v. Public Utilities Commission, 67 Ohio St.2d 372, 424 N.E.2d 300 (1981). The Supreme Court held on this issue:

> "Inasmuch as we have already determined that the Commission improperly allowed amortization of the utility's investment in the terminated nuclear facilities, it is unnecessary for us to address the timing issue raised in this cause."
>
> Consumers' Counsel, et al. supra, at p. 167, 423 N.E.2d at 828.

On July 15, 1981, the Supreme Court of Ohio held that the Commission had exceeded its statutory authority in allowing the expenses related to the unbuilt power plants since these costs were not related to providing utility service to the consumer during the test period and, therefore, did not qualify for inclusion under Ohio's statutory ratemaking law, Section 4909.15 Ohio Revised Code. The Court expressly noted (consistent with CEI's arguments before the Court):

> "The controversy surrounding the cancelled nuclear power plants focuses primarily on R.C. 4909.15(A)(4) which delineates the service-related costs that a utility may recover from its ratepayers."
> Consumers' Counsel, et al., at p. 163, 423 N.E.2d at 826.

The Supreme Court's holding was consistent with prior interpretations by the Ohio Court in numerous cases disallowing expenses related to "past losses" and holding that property may be included for rate-

making purposes only if either "used and useful" in rendering utility service to the public or 75% complete as construction works in progress. See Columbus and Southern Ohio Electric Co. v. Public Utilities Commission, 64 Ohio St.2d 175, 413 N.E.2d 1208 (1980), cert. denied, __ U.S. __, 101 S. Ct. 3071 (1981); Consumers' Counsel v. Public Utilities Commission, 58 Ohio St.2d 449, 391 N.E.2d 311 (1979); City of Cleveland v. PUC, 63 Ohio St. 2d 62, 406 N.E.2d 1370 (1980). All parties conceded that these plants were neither "used and useful" nor 75% complete.

After the Ohio Supreme Court announced its decision in July, CEI for the first time raised its alleged constitutional arguments in a Motion for Rehearing before the Ohio Court. Consistent with Ohio Supreme Court practice, which mandates that rehearing will not be allowed merely to assign new errors not brought to the atten-

tion of the Court at the original hearing, the Ohio Supreme Court denied CEI's Motion for Rehearing without opinion. See Cincinnati v. Cameron, 33 Ohio St. 336 (1878), 5 Ohio Jurisprudence 3rd, Appellate Review § 510, p. 59 (1978). CEI, in its present appeal, now raises before this Court constitutional claims not presented to the Court below prior to its decision in the instant case.

III. ARGUMENT

A. THIS COURT LACKS JURISDICTION BECAUSE APPELLANT FAILED TO TIMELY RAISE ITS ALLEGED CONSTITUTIONAL QUESTIONS IN THE COURT BELOW.

1. CEI Did Not Raise Any Constitutional Claims In Its Initial Brief or Oral Argument Before the Ohio Supreme Court.

It is a fundamental policy of this Court that, in order to exercise jurisdiction on appeal, "there be an explicit and timely insistence in the state courts that a state statute, as applied, is repugnant to the federal Constitution, treaties or laws." Charleston Federal Savings & Loan Association v. Alderson, 324 U.S. 182, 185 (1944)(emphasis supplied). The standard as to what constitutes an "explicit and timely insistence" has been clearly delineated by this Court. Although no particular form of words is necessary, this Court has held that "there yet must be something in the case before the state

court which at least would call its attention to the Federal question as one that was relied on by the party . . ." Dewey v. Des Moines, 173 U.S. 193, 199 (1899) (emphasis supplied). Only then can the issue be deemed to be raised 'with fair precision and in due time.' New York, ex rel. Bryant v. Zimmerman, 278 U.S. 63, 67 (1928).

The particular rules of the state courts are to be utilized in determining whether a constitutional claim has been timely raised and relied upon by the appellants for purposes of appeal. Beck v. State of Washington, 369 U.S. 541, 549-533 (1962). In the instant case, the Ohio Supreme Court has promulgated clear rules as to how an appellant or appellee must present a legal argument it seeks to rely upon. Ohio Supreme Court Rule of Practice V(D) provides that each argument must be in the form of a proposition of law with appro-

priate heading and subheading. The rules mandate that a party must set forth a statement of the rules of law which he contends are applicable to the facts of the case. Drake v. Bucher, 5 Ohio St. 2d 37, 213 N.E. 2d 182 (1966) (Syllabus 3).

At no time did CEI, as intervening Appellee before the Ohio Supreme Court, even mention, let alone argue, any "constitutional issues" before the Ohio Supreme Court in either its initial brief or oral argument. The propositions of law and subpropositions presented by CEI to the Ohio Court on brief were limited to arguments involving the interpretation of Ohio statutes.[3]

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[3] For example, CEI's second subheading, in which the lawfulness of the Commission's action was discussed, stated:

"There is no question but

CEI alleges, in its Jurisdictional Statement, page 10, that it "alerted" the Ohio Court to the possibility that a constitutional issue "might arise". The claimed "alert" consisted of a citation, in support of another proposition of law, to a case which, in a dissenting opinion, makes vague reference to "constitutional" rights to "just compensation." The emphasis supplied to these words in CEI's Jurisdictional Statement, page 11, was not supplied in its brief to the Ohio Court. On the contrary, CEI cited the case along with others in support of its proposed interpretation of Ohio's statutes. The

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that the Ohio statutory framework permits recognition of the expenses here in question for rate making purposes." CEI brief at p. 16.

portion of the case cited which refers to the constitutional issue which CEI now wishes to rely on was not even called to the attention of the Ohio Court by underlining or otherwise. There was certainly no indication whatsoever that CEI wished to rely upon it. (See Dewey v. Des Moines, supra). CEI never even framed the proposition of law it now alleges is implicit in this vague reference. Surely CEI is not proposing that the Ohio Court should bear the impossible burden of having to comb every citation utilized by counsel to find issues, not raised by parties, which could possibly be relevant to the proceeding. If CEI thought there were "substantial constitutional questions" in this proceeding, it surely would have done far more than merely make oblique reference to

them through citations to dissenting opinions.[4]

A direct affirmative effort of "fair precision" in the Court below is required in order to properly raise an alleged constitutional issue to this Court on appeal from a state court ruling. New York, ex rel. Bryant v. Zimmerman, 278 U.S. 63, 67 (1928). In the instant case no effort at all was made. Supreme Court Rule 16(1)(b) mandates that this appeal be dismissed.

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[4]It is worthy to note that, although CEI now premises its appeal to this Court on alleged conflict between the Ohio Court's ruling and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), this case was never cited by Appellant, not even in its Motion for Rehearing to the Ohio Court where CEI first asserted a constitutional claim.

2. CEI Cannot Claim "Suprise" By The Holding Of The Ohio Supreme Court, and Was Not, Therefore, Entitled To Raise The Federal Question On Motion For Rehearing To That Court.

CEI claims that, even if the constitutional issue was not raised during the appeal, CEI was "surprised" by the holding of the Ohio Supreme Court and was thus entitled to raise the constitutional issue on a Motion for Rehearing. This contention is simply unsupportable in the instant case. It is true that, in certain limited instances, this Court has permitted a Federal question to be raised, even though such question was not raised until a Motion for Rehearing. See, Pruneyard Shopping Center v. Robbins, 447 U.S. 74, 86 fn. 9 (1980). Such instances are limited to those cases "when the highest state court renders an unexpected interpretation of state law or reverses its prior interpretation." Pruneyard, supra, at p. 86, fn. 9.

In the instant case, it is clear that the Ohio court did not "reverse its prior interpretation" of state law such as to "surprise" CEI, nor was its ruling "unexpected". Although the specific fact situation presented to the Commission and the Court had not been ruled upon in any prior Ohio decision, the Court merely applied well established precedent in Ohio utility law to the facts of the instant case. There is an abundance of Ohio precedent for the Court's ruling that utility property and expenses associated therewith cannot be recovered through rates unless the property is both dedicated to service for the public and used and useful to it. See e.g. East Ohio Gas Co. v. Public Utilities Commission, 133 Ohio St. 212, 12 N.E. 2d 765 (1938); Consumers' Counsel v. Public Utilities Commission, 58 Ohio St. 2d 449, 391 N.E.2d 311 (1979). CEI was fully aware of the long line of precedent which holds

that Ohio utilities cannot recover past losses through future rates. Columbus & Southern Ohio Electric Co. v. Public Utilities Commission, 64 Ohio St.2d 175, 413 N.E.2d 1208 (1980) cert. denied, __ U.S. __, 101 S. Ct. 3071 (1981). As noted by Ohio Supreme Court Justice Locher in his concurring opinion, CEI anticipated that the costs related to the cancelled plants might be disallowed, as evidenced by the following statement in CEI's 1979 Annual Report To Shareholders:

> "The extent to which these costs may be recovered through rates will be determined by the PUCO. If any costs of termination are not permitted to be recovered, the Company would be required to reduce Net Income by the disallowed amount. In any event, the resolution of these matters should not have a material adverse impact on the financial position of the Company."
> Consumers' Counsel, et al., supra, at p. 171, Justice Locher concurring.
> (emphasis supplied)

Under these circumstances it can hardly be

said that CEI's counsel can be excused for having failed to timely raise below the alleged constitutional issues it now asks this Court to entertain.

B. THIS COURT LACKS JURISDICTION BECAUSE APPELLANT HAS FAILED TO RAISE ANY CONSTITUTIONAL ISSUE.

CEI raises two arguments de novo in support of its allegation that the Ohio Court's decision should be set aside on constitutional grounds.[5]

Appellant's first argument amounts to little more than the bare proposition that the disallowance by a rate Commission of any expense (whether related to the rendition of service or not) leads to a confiscatory result. Such a proposition com-

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[5] We say de novo because Appellant never cited Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944) to the Ohio Supreme Court upon which it now relies as one of its grounds for plenary consideration by this Court.

pletely misstates the law of both Ohio and the United States. The Constitution does not guarantee that every expense of a utility, whether recurring or not, must be borne by the ratepayer. Utility investors are not guaranteed to be shielded from all risk of loss. CEI's arguments on these points were expressly rejected by this Court over fifty years ago in Bluefield Waterworks v. Public Service Commission, 262 U.S. 679 (1923). Bluefield specifically holds that the United States Constitution entitles a utility only to:

> "(r)ates which are . . . sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service . . . the Company may not insist as a matter of constitutional right that past losses be made up by rates to be applied in the present and future." Bluefield, supra, at 690, 694 (emphasis supplied).

It is undisputed that these

planned but unbuilt plants provided no service to the consumer. The issue before the Ohio Court was whether the Ohio legislature, in enacting Title 49 Ohio Revised Code, intended to grant utilities the right to recover expenses beyond the minimum prescribed by the United States Constitution. The Ohio Supreme Court, in interpreting the Ohio statutes and legislative intent, found it had not:

> "The statutes in question contain no provisions insulating investors from the type of losses sustained in the cancelled plants venture."
> Consumers' Counsel, et al., supra at p. 167, 423 N.E.2d at 829.

The issue is strictly a question of Ohio state law and state policy. Whether the utility is seeking a return "of" or "on" its property, it is clear that, as a matter of Federal Constitutional law, such

property must first be dedicated to the public service.[6]

In its second argument, Appellant asserts that the Ohio Court's decision is somehow in conflict with Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944). It is odd that Appellant seeks to rely on the Hope decision as that

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[6]Appellant's argument that the investor must recover his investment whether or not it provided service to the public would put utility investors in a superior position to persons investing in nonregulated industries. Their investment would essentially become risk free -- a proposition expressly rejected by this Court in Bluefield. As stated in Washington Gas & Light Co. v. Baker, 188 F. 2d 11, 20 (D.C. Cir. 1950) cert. denied, 340 U.S. 952 (1951), wherein costs of abandoned facilities were disallowed:

> "The effect upon the consumer would be the same as if an insured person were required to assume the loss against which he believed himself protected by payment of premiums. The result would clearly violate the consumers' interest against exorbitant rates."

case is more supportive of Appellees' position than its own. In Hope, this Court adopted an "end-result" test in judging whether a utility rate order is confiscatory:

> "It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important . . . And he who would upset the rate order under the Act carries the burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences." Hope, supra, at p. 602.

In the instant case, although Appellant claims that its rates are not now earning a proper return and that the application of the Ohio Court's decision is, therefore, confiscatory, CEI has not sought the remedy of emergency rate relief available to it under Ohio law. Section 4909.16 Ohio

Revised Code. Its failure to do so is additional evidence that, in fact, "the (adverse) resolution of these matters (disallowance of the planning expenses) should not have a material adverse impact on the financial position of the Company", as CEI stated in its 1979 Annual Report to Shareholders. Consumers' Counsel, et al., at p. 171.[7]

Complex issues as to what rate of return CEI is now earning (CEI brief at pp. 18-19) are not a proper subject for this Court's review on the basis of bare assertions by counsel on brief. The State Commission is the proper ratemaking body where

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[7] Testimony by CEI and Commission staff witnesses in the proceedings before the Commission in the instant case also established that the risk of noninclusion of property and costs associated with property found not to be "used and useful" in the rendering of service is a risk anticipated by investors, who are thus compensated through rate of return.

the issues are resolved through the testimony of experts subject to cross-examination by Appellees and the Commission staff. CEI can cite to no evidence in the record that the "end-result" of the Court's decision to disallow $6.5 million of expense out of total allowable gross annual revenues of $843 million authorized by the Commission in the instant case renders the end-result confiscatory under Hope.[8]

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[8]It should be noted that CEI has applied to the Commission for a $130 million rate increase in which CEI has expressly requested an increased rate of return to compensate for the allegedly unrecovered losses resulting from the Ohio Court's decision in the instant case. Hearings on this case are scheduled to begin within two weeks of the writing of this Brief.

C. APPELLANT'S CLAIMS INVOLVE MATTERS OF PURELY LOCAL INTEREST.

Appellant urges this Court to consider decisions of various regulatory agencies of other states which have allowed recovery for expenses associated with terminated plants.[9] These decisions, although interesting for their reasoning in applying various state laws, are clearly irrelevant to the instant appeal from the decision of the Ohio Supreme Court. The Ohio Court clearly stated that its decision was limited to questions of Ohio statutory law:

> ". . .It is important to note that none of the previous rulings on this precise issue represents the opinion of the highest court of the jurisdiction in which the case arose . . .

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[9] In at least two states the utility's request for recovery of these costs has been denied. This Appellee knows of no appeal taken from these agency decisions to state courts. See, Re Arizona Public Service Co., Decision No. 51009 (Arizona Corp. Comm. 1980); Re Northern States Power Co., Case No. 10097 (Pub. Ser. Comm. of N.D. 1980).

> Even more significant is the fact that no other case has considered the propriety of the Commission's proposed amortization with reference to Ohio law . . . The construction of Ohio law is particularly the province of this court and we are nowise bound by the pronouncements of regulatory regimes elsewhere in effect." Consumers' Counsel, et al. supra, at p. 162-163, 423 N.E.2d at 826. (emphasis supplied.)

None of the jurisdictions cited by CEI whose local commissions have decided this issue have a ratemaking formula which includes language even closely approximating that embodied in Ohio Revised Code Section 4909.15.

Appellant cites to a variety of jurisdictions, including four state courts, where cases are presently pending which involve the issue of recovery of expenses similar to those disallowed under Ohio law in the instant case (See Exhibit 1, CEI Jurisdictional Statement). Each of these local state commissions or courts will,

of course, decide whether its applicable state law allows such recovery. The decision by the Ohio Court in the instant case has no relevance outside Ohio and, therefore, no bearing on these decisions. So long as the minimum guarantees under the United States Constitution as propounded in Bluefield Waterworks v. Public Service Commission, supra, are satisfied, each state is free to allow or disallow additional expenses as its ratemaking philosophy, expressed through its legislature, may dictate.

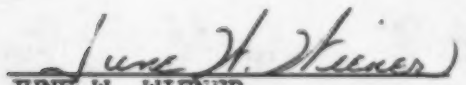
In addition to the procedural and substantive bars to this Court's jurisdiction, the purely local impact of the instant case makes it an improper and inappropriate vehicle for this Court's exercise of jurisdiction.

IV. CONCLUSION

For the above-stated reasons the City of Cleveland, Ohio respectfully moves for dismissal of the instant appeal.

Respectfully submitted,

JAMES E. YOUNG
DIRECTOR OF LAW

By: 
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APPENDIX

§ 4903.10 Rehearing.

After any order has been made by the public utilities commission, any party who has entered an appearance in person or by counsel in the proceeding may apply for a rehearing in respect to any matters determined in said proceeding. Such application shall be filed within thirty days after the entry of the order upon the journal of the commission.

Notwithstanding the preceding paragraph, in any uncontested proceeding or, by leave of the commission first had in any other proceeding, any affected person, firm, or corporation may make an application for a rehearing within thirty days after the entry of any final order upon the journal of the commission. Leave to file an application for rehearing shall not be granted to any person, firm, or corporation who did not enter an appearance in the proceeding unless the commission first finds:

(A) The applicant's failure to enter an appearance prior to the entry upon the journal of the commission of the order complained of was due to just cause; and,

(B) The interests of the applicant were not adequately considered in the proceeding.

Every applicant for rehearing or for leave to file an application for rehearing shall give due notice of the filing of such application to all parties who have entered an appearance in the proceeding in the manner and form prescribed by the commission.

Such application shall be in writing and shall set forth specifically the ground or grounds on which the applicant considers said order to be unreasonable or unlawful. No party shall in any court urge or rely on any ground for reversal, vacation, or modification not so set forth in said application.

. . . . . .

Where such application for rehearing has been filed before the effective date of the order as to which a rehearing is sought, the effective date of such order shall, unless otherwise ordered by the commission, be postponed or stayed pending disposition of the matter by the commission or by operation of law. In all other cases the making of such an application shall not excuse any person from complying with the order, or operate to stay or postpone the enforcement thereof, without a special order of the commission.

Where such application for rehearing has been filed, the commission may grant and hold such rehearing on the matter specified in such application, if in its judgment sufficient reason therefor is made to appear. Notice of such rehearing shall be given by registered mail to all parties who have entered an appearance in the proceeding.

If the commission does not grant or deny such application for rehearing within thirty days from the date of filing thereof, it is denied by operation of law.

Where the commission grants such rehearing, it shall specify in the notice of such granting the purpose for which it is granted. The commission shall also specify the scope of the additional evidence, if any, which will be taken, but it shall not upon such rehearing take any evidence which, with reasonable diligence, could have been offered upon the original hearing.

If, after such rehearing the commission is of the opinion that the original order or any part thereof is in any respect unjust or unwarranted, or should be changed, the commission may abrogate or modify the same; otherwise such order shall be affirmed.

An order made after such rehearing, abrogating or modifying the original order shall have the same effect as an original order, but shall not affect any right or the enforcement of any right arising from or by virtue of the original order prior to the receipt of notice by the affected party of the filing of the application for rehearing.

No cause of action arising out of any order of the commission, other than in support of said order, shall accrue in any court to any person, firm, or corporation unless such person, firm, or corporation has made a proper application to the commission for a rehearing.

§ 4909.16 Power to amend, alter, or suspend schedule of rates. (GC § 614-32)

When the public utilities commission deems it necessary to prevent injury to the business or interests of the public or of any public utility of this state in case of any emergency to be judged by the commission, it may temporarily alter, amend, or, with the consent of the public utility concerned, suspend any existing rates, schedules, or order relating to or affecting any public utility or part of any public utility in this state. Rates so made by the commission shall apply to one or more of the public utilities in this state, or to any portion thereof, as is directed by the commission, and shall take effect at such time and remain in force for such length of time as the commission prescribes.

Section 7. Form of Copies

Copies of portions of the record, testimony and exhibits filed pursuant to this rule must conform with the requirements of Rule VI.

Rule V

BRIEFS ON MERITS IN APPEAL CASES

Section 1. Appellant's Brief

The appellant in all civil cases must file eighteen copies of a brief within ten days of the date the copies of the record are filed with the Court. The appellant in all criminal cases must file eighteen copies of a brief within forty days of the date of the allowance of the appeal.

The appellant's brief must comply with Rule VI and contain:

(A) A table of contents listing the table of authorities, statement of facts, argument (with the proposition or propositions of law and authorities relied upon to support the same) and appendix, all as required by the following subparagraphs of this rule, with references to the pages of the brief where each appears, and arranged as shown by the following sample:

[SAMPLE]

TABLE OF CONTENTS.

Page No.

TABLE OF AUTHORITIES [if required, see Section 1(B) of this rule.] 1

STATEMENT OF FACTS 2

[May be divided between statement of the case and statement of facts. Appellee should confine his statement to differences between the parties or to additional material.]

ARGUMENT 3

[Sample proposition of law taken from first paragraph of syllabus of Bureau of Support v. Kreitzer (1968), 16 Ohio St.2d 147, 243 N.E.2d 83.]

Proposition of Law No. 1:

The duty of the state of Ohio to support inmates (or patients) of benevolent institutions under the jurisdiction of the Department of Mental Hygiene and Correction,

Page No.

as set forth in R.C. 5121.01, is qualified by R.C. 5121.03 *et seq.*, so that the nature of its liability for support is secondary. Primary liability for such support, at least in the case of a patient without dependents, rests absolutely upon the patient himself, by virtue of R.C. 5121.-04(B) (1), or upon his estate. 3

Authorities cited in support of Proposition of Law No. 1: [in the order in which they appear in the brief]

State, ex rel. Price v. Huwe (1922), 105 Ohio St. 304, 137 N.E. 167 3

State v. Kleeswetter (1882), 37 Ohio St. 546 3

R.C. 5121.01 4

R.C. 5121.10 4

R.C. 5121.04(B) (1) 4

R.C. 5121.03 5

Lackmann v. Dept. of Mental Hygiene, 156 Cal.App.2d 674, 320 P.2d 186 5

[If desired, the argument under each Proposition of Law may be subdivided. Appellee shall state the proposition in the form which would, if adopted, support judgment in his favor.]

Proposition of Law No. 2 7

[State with successive numbers, each, if any, additional propositions relied upon.]

APPENDIX

Notice of Appeal to the Supreme Court 9

Assignment of error filed in the Court of Appeals 10

Opinion of the Court of Appeals 11

Journal Entry of the Court of Appeals 13

Opinion of the Court of Common Pleas (or BTA or PUCO) 14

Journal Entry of the Court of Common Pleas (or BTA or PUCO) 16

R.C. 5121.01 17

R.C. 5121.03 17

R.C. 5121.04 19

R.C. 5121.10 19

[Note: All of the above mentioned documents must be included in the appellant's brief. They shall not be repeated in the printed record or appellee's brief.]

(B) If the total number of separate citations exceeds twelve (12), a table of authorities listing all cases or other authorities, arranged alphabetically, and all statutes, constitutional provisions, and departmental, board or commission regulations relied upon, with references to the pages of the brief where each citation appears.

(C) A statement of the facts with page references, in parentheses, to supporting portions of the printed or nonprinted record and of the original transcript of testimony. (Obviously, in a memorandum under Rule II, Section 4, references to a printed or nonprinted record cannot be made.)

(D) An argument, which shall be headed by the proposition of law which the appellant contends is applicable to the facts in the case and which, if he prevails, could serve as a syllabus. See paragraph three of the syllabus of Drake v. Bucher, Supt. (1966), 5 Ohio St.2d 37, 213 N.E.2d 182. If several propositions of law are contended for, the argument shall be divided by utilizing each proposition as a subheading.

(E) An appendix containing (a) a copy of the notice of appeal to the Supreme Court, (b) a copy of the assignments of error filed in the Court of Appeals, (c) a copy of the judgment or order appealed from, (d) copies of all judgments, orders, and opinions rendered by any court or board in the case, (e) complete copies of any unreported cases cited, (f) the rules or regulations of any department, board, commission or any other agency relied upon (such rules shall be set forth in full, or if too voluminous, a copy thereof shall be furnished with each copy of the brief), and (g) a copy of any statute or constitutional provision relied upon, to be construed or otherwise involved in the case. The pages of the appendix shall be numbered.

(F) If it is necessary to file multiple appeals from a single decision of a Court of Appeals or an administrative agency and such appeals are docketed under separate case numbers, counsel for the appellants should, whenever possible, file a single brief or memorandum for all such appeals. The cover page of such brief or memorandum should contain the names and numbers of each case.

Section 2. Brief Opposing Appeal

Within thirty days of the filing of appellant's brief, the party opposing the appeal shall file a brief in form complying with the provisions of this rule and Rule VI and answering the appellant's contentions and making any other contentions deemed appropriate as reasons for affirmance of the order or judgment appealed from.

Section 3. Reply Briefs

Any reply brief must be filed within twenty days after the filing of appellee's brief and must comply with Rule VI as to form.

Section 4. Additional Authorities

In all cases where the briefs filed in compliance with these rules do not contain all the authorities on which counsel intends to rely, there must be filed a brief statement of additional authorities. This statement should be filed at least five days before oral argument.

Section 5. Briefs Amicus Curiae

Briefs amicus curiae conforming to the requirements of this section may be filed with leave of Court. Any amicus curiae shall file its brief within the time allowed the party whose position as to affirmance or reversal the amicus brief will support.

Section 6. Proof of Service

Service of a copy of each brief or statement of additional authorities shall be made upon opposing counsel forthwith, and proof of service shall be filed with the Clerk.

Section 7. Additional Docket Fee Where Appeal Allowed

Where a motion to certify has been allowed, or motion for leave to appeal has been granted, the appellant must pay an additional docket fee of five dollars on the filing of his brief.

Amended Jan. 6, 1975; June 20, 1977.

Motion to Dismiss or Affirm

2

Office-Supreme Court, U.S.
FILED
DEC 30 1981
ALEXANDER L. STEVAS,
CLERK

Case No. 81-1002

In the Supreme Court of the United States

October Term, 1981

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

Appellant,

vs.

OFFICE OF CONSUMERS' COUNSEL, SENIOR CITIZENS COALITION, GREATER CLEVELAND WELFARE RIGHTS ORGANIZATION, INC., WESTERN RESERVE ALLIANCE, NORTH SHORE ALERT, CLEVELAND CHAPTER OF OHIOANS FOR UTILITY REFORM,

and

THE PUBLIC UTILITIES COMMISSION OF OHIO,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF OHIO

MOTION TO DISMISS

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TABLE OF CONTENTS

	Page
Table of Authorities ----------	ii
Statement of Case ----------	1
Reason Requiring a Dismissal of the CEI Appeal ----------	14
WHEN AN APPELLANT UTILITY COMPANY HAS FAILED TO RAISE TIMELY AND PROPERLY FEDERAL QUESTIONS ALLEGING CONFISCATION OF ITS PROPERTY AND SUCH QUESTIONS WERE NOT EXPRESSLY PASSED UPON BY A STATE COURT, AN APPEAL RAISING THESE QUESTIONS WILL BE SUBJECT TO A MOTION TO DISMISS, UNDER REVISED RULE 16 OF THE SUPREME COURT OF THE UNITED STATES.----	14
Conclusion ----------	33
Appendix ----------	35

TABLE OF AUTHORITIES

CASES

	Page
Federal Power Commission v. Hope Natural Gas Company 320 U.S. 591 (1944)	16
Street v. New York, 394 U.S. 576 at 583, 89 S. Ct. 1354 at 1361 (1969)	20
New York ex rel Bryant v. Zimmerman, 278 U.S. 63 at 67, 49 S. Ct. 61 at 63 (1928)	21
In Re Cleveland Electric Illuminating Company, PUCO 80-376-EL-AIR	22
Cardinal v. Louisiana, 394 U.S. 437 at 439, 89 S. Ct. 1161 at 1163 (1969)	25
Crowell v. Randell, 10 P. 368 at 391-2, 12 Curtis 164 at 165-6 (1836)	27
Quilloin v. Walcott, 434 U.S. 246 98 S. Ct. 549 (rehearing denied- 435 U.S. 918, 98 St. Ct. 1477) (1978)	28
Brown v. Aspden, 14 How 25 (1852)	29
Longworth & Horen v. Sturges & Anderson, 2 O. St. 105 at 107-8 (1853)	30
Edelman v. People of State of Cal., 344 U.S. 357, 73 S. Ct. 293 (1953)	33

CASES

Page

Spies v. Illinois, 123 U.S. 131
8 St. Ct. 21 (1887) ---------- 33

St. Louis and San Francicso
Railroad Co. v. Shepherd
240 U.S. 240, 36 S. Ct. 274
(1916) ---------- 33

McMillen v. Ferrum Mining Company
197 U.S. 343, 25 S. Ct. 533
(1905) ---------- 33

STATUTES

U. S. Supreme Court Rule 16(1)(b)- 17, 28

Ohio Supreme Court Rule V,
Section 2 ---------- 22

Ohio Supreme Court Rule V,
Section 1(D) ---------- 23

Ohio Supreme Court Rules of
Practice, Rule IX ---------- 30

O.R.C. Section 4909.15 ---------- 5

OTHER AUTHORITIES

Appellate Review, Section 510,
5 O. Jur. 3d (1978)---------- 31

STATEMENT OF THE CASE

On January 23, 1980, Appellant, the Cleveland Electric Illuminating Company ("CEI"), announced the decision to cancel and abandon plans for the construction of four nuclear generating plants. Almost from the very beginning in early 1973 when CEI along with four other electric utilities had first stated plans to build these four units, there were utility consumers and citizen organizations that strongly questioned the wisdom of such construction, both on the grounds of safety and need.

At the time when CEI announced the decision to cancel, the Company also had pending before the Public Utilities Commission of Ohio ("PUCO") an application for a general increase in rates. CEI now sought to add its costs of some $56,437,000 for the planning,

engineering, and initial construction of the four terminated plants to this general rate case. Specifically, CEI requested that it be allowed to amortize its costs over a ten-year period, thus charging its customers for plants that would never produce a kilowatt of electricity.(1)

CEI was well aware that it needed legal approval for such amortization. Moreover, the Company had indicated to

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(1) CEI in its "Jurisdictional Statement" points out that it was only attempting to seek a "recovery of investment" rather than any additional return on" its investment, which the company says has been allowed in some other jurisdictions. The implication is that Ohio consumers should be satisfied with this compromise. This very argument, however, exposes the weakness of the Appellant's legal position. The issue is what basis is there under Ohio law to pass such costs for cancelled plants--whether "of" or "on" investment--onto utility customers.

its stockholders that such amortization might not be allowed. CEI's own public statement in its 1979 Annual Report which was issued shortly after the announcement of the plants' cancellation contains the following analysis and assurances:

> The Company has invested approximately $60 million in preliminary work for the four units terminated. Contractors may claim additional charges. A significant portion of all of these costs will be claimed as a tax deduction. The Company will seek the approval of the Federal Energy Regulatory Commission and The Public Utilities Commission of Ohio for authority to amortize these costs over a suitable number of years. The extent to which these costs may be recovered through rates will be determined by the PUCO. If any costs of the termination are not permitted to be recovered, the Company would be required to reduce Net Income by the disallowed amount. In any event, the resolution of these matters should not have a material adverse impact on the financial position of the Company. (Emphasis supplied.)

Since this CEI request for amortization was presented so late in the proceedings and because of its unusual nature, various intervenors including the Appellees, Senior Citizens Coalition, the Greater Cleveland Welfare Rights Organization, Inc., Western Reserve Alliance, North Shore Alert, and the Cleveland Chapter for Ohioans for Utility Reform objected vigorously to any such special treatment. At the public hearing of this case on April 2, 1980, citizen consumers of CEI as well as public officials testified before the PUCO and argued strenuously that customer rates should not include any costs connected with the four cancelled plants.

Throughout the PUCO hearings there was no dispute that the four cancelled nuclear plants provided no service to CEI customers during the "test year" which was the basis for the Appellant's

original request for rate relief. There was no dispute that these four cancelled nuclear plants would never provide any service and thus would never be "used and useful" so as to qualify for rate base treatment in calculating customer rates. There was no dispute that these four barely begun plants did not qualify for treatment as "Construction Work in Progress" since Ohio's law requires as one of its preconditions that facilities must be "at least seventy-five percent complete" before they can be charged to customers as part of rate base. (See Ohio Revised Code Section 4909.15.)

At the conclusion of the hearings, extensive briefs were submitted by Appellant CEI as well as by all of the Appellees on the four cancelled plants and other issues. On July 10, 1980 the PUCO released its "Opinion and Order" which granted CEI almost $70 million of

the approximately $80 million increase sought by the Company. Included in this was a yearly allowance of some $7 million representing the ten-year amortization of costs connected with the four terminated plants.

While the PUCO did allow the amortization, its "Opinion and Order" reflects the Commission's own doubts about its ruling. "The real threshold question here," declared the Opinion and Order, "which the Commission perceives as the most difficult of all the issues raised in connection with the matter, is whether this adjustment is legally permissible...." (Emphasis supplied; see D-53 and 54 of CEI's Appendix.) Moreover, the Commission recognized that its past pronouncements had established the principle of "the impropriety of the recovery of past losses through future rates." Despite

this principle the PUCO tried to distinguish the announcement of cancellation of the plants as "not creat[ing] a past loss, but giv[ing] rise to a current cost," although the $56,437,000 had been spread over the seven past years.

After the "Opinion and Order," all seven of the Appellees--the Ohio Consumers Counsel, the Senior Citizens Coalition, et al, and the City of Cleveland--timely filed for a rehearing, contending that the PUCO had improperly and illegally allowed the amortization. After these requests were denied by the PUCO, three separate appeals were taken to the Supreme Court of Ohio. The one common issue in all three appeals was the question of amortizing the costs connected with the four terminated nuclear plants.

Lengthy briefs were presented by CEI and the Attorney General Counsel for the PUCO in favor of the PUCO's decision while the Appellees submitted briefs in opposition. All three appeals were heard the same day before all seven justices of the Court. Since there were three separate appeals, the amount of time available for oral argument and exploration on both sides of this controversy turned out to be substantially more than is ordinarily allotted on appeals to Ohio's highest court.

On July 10, 1981, the Supreme Court of Ohio, in a 5-2 decision, reversed the PUCO. The Supreme Court examined every basis of Ohio law offered by both CEI and the Attorney General Counsel for the PUCO as alleged justification for the latter's decision. The Court found that none of these provided sufficient legal basis for the amortization. (See the

Court's discussion at C-11 to 18 of CEI's Appendix.) The Court then pointed out that under a long series of Ohio cases the PUCO "may not legislate in its own right." The Court is quite specific in its holding which was foreshadowed by the PUCO itself in its original Opinion and Order:

> The commission order engrafts upon the statutory ratemaking scheme an exception that would allow utility companies to re-recover their investment in unfinished projects ineligible for rate base treatment if the original decision to build the facilities and the subsequent decision to cancel the projects are prudent under the circumstances. In so doing the commission has exceeded its statutory mandate. We hold that the commission unreasonably and unlawfully exceeded it statutory authority when its approved amortization of CEI's investment in the four terminated nuclear power plants. (See page C-18 of CEI's Appendix.)

The Ohio Supreme Court then suggested that if times were so "parlous" for the utilities industry that companies

"must also be assured the return of capital invested in failed projects that would otherwise not be recoverable under the [Ohio] ratemaking formula," then appeals should be made to the Ohio Legislature to enact such changes. Indeed, the Legislature has responded to utility problems in the past. In 1976, for example, the Legislature had amended the Ohio Revised Code to allow utility companies faced with financial problems involving the building of new large facilities to include "Construction-Work-in-Progress" or "CWIP" costs for rate base treatment under various circumstances even though such projects were not yet serving customers.

After the decision was announced, CEI filed a Motion for Rehearing on July 24, 1981. This was the first time that the Appellant CEI had explicitly

raised any Federal question arguments that somehow Ohio customers are forced under the Constitution to reimburse CEI and its investors for these four terminated nuclear plants which the Appellant had originally chosen to construct but which never have and never will furnish customers a single kilowatt of energy. The Ohio Supreme Court on September 1, 1981, issued the Court's mandate and denied the Motion for Rehearing without any written opinion.

On September 22, 1981, CEI filed with the United States Supreme Court an Application for Stay of Execution and Enforcement of the Judgment of the Supreme Court of Ohio. (See Case No. A-250.) Subsequently, the Senior Citizens Coalition, et al, as well as the other Appellees and CEI filed briefs. On October 12, 1981, this Court denied the requested stay.

Meanwhile, the PUCO finally was beginning to take some action in an attempt to obey the Ohio Supreme Court's mandate. A new case was begun by the PUCO itself which on October 21, 1981 resulted in decreasing the monthly electric bills for CEI's customers, including hard-pressed senior citizens and families forced by social circumstances to live on low and fixed incomes. Unfortunately, the PUCO order was prospective only and CEI so far has been allowed to keep almost $10 million collected from its customers based upon the prior rates which included the amortization for the four cancelled plants.

On November 25, 1981, CEI filed its Jurisdictional Statement and a separate Appendix. The Senior Citizens Coalition, the Greater Cleveland Welfare Rights

Organization, Inc., Western Reserve Alliance, North Shore Alert, and the Cleveland Chapter of Ohioans for Utility Reform are convinced that an appeal to the U.S. Supreme Court on the federal questions proposed by the Appellant is unnecessary and improper. They, therefore, join together in filing this Motion to Dismiss.

REASON FOR REQUIRING A DISMISSAL OF THE CEI APPEAL

WHEN AN APPELLANT UTILITY COMPANY HAS FAILED TO RAISE TIMELY AND PROPERLY FEDERAL QUESTIONS ALLEGING CONFISCATION OF ITS PROPERTY AND SUCH QUESTIONS WERE NOT EXPRESSLY PASSED UPON BY A STATE COURT, AN APPEAL RAISING THESE QUESTIONS WILL BE SUBJECT TO A MOTION TO DISMISS UNDER REVISED RULE 16 OF THE SUPREME COURT OF THE UNITED STATES.

In its Jurisdictional Statement, CEI has stated two reasons why this case requires plenary consideration. These two reasons and Appellant's asserted Constitutional rights rest upon highly debatable legal and factual propositions.(2) But it is not necessary to

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(2) Such propositions include the following:

First, to the extent that Appellant's distinction between a return of capital as to on capital suggests that a utility is guaranteed every dollar of invested capital will be returned, such a distinction is false.

Footnote No. 2 continued:

Second, to the extent that Appellant is suggesting it and its stockholders were forced by Ohio law to construct these four plants, such a suggestion has no basis in law or fact.

Third, Appellant now expresses a surprise that a legal decision would not allow amortization of the costs connected with the four plants. (See pages 16, 17, and 22 of CEI's Jurisdictional Statement.) Yet this possibility was explicitly addressed in the Company's already quoted 1979 Annual Report.

Fourth, although Appellant's contentions that its capital has been confiscated is a very serious charge, this hardly comports with CEI's statement to its stockholders in its 1979 Annual Report that, "In any event [whether the costs are allowed to be amortized or are not permitted to be recovered], the resolution of these matters should not have a material adverse impact on the financial position of the company." In his concurring opinion Justice Locher of the Ohio Supreme Court specifically pointed to this passage in concluding "the financial effect of this decision on CEI will be insignificant." (See page C-23 and 24 of CEI's Appendix.)

Fifth, Appellant's motion that its investors, which would include those owning common stock, must be compensated virtually in advance for every particular risk is at least debatable. The very idea of "risk" contains the notion of the unknowable which may well include the possibility that investment in planned construction may never be chargeable to customers because it never benefits them.

Sixth, if CEI was telling the truth in its 1979 Annual Report that disallowance of the expenditures for the four cancelled plants "should not have a material adverse impact on the financial position of the Company."

Footnote No. 2 continued:

there does not seem to be any reason to alter the rate of return or increase compensation to investors for this allegedly unassumed risk. Furthermore, any invocation of Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), seems superfluous.

Seventh, CEI's argument for confiscation is based upon evidence and calculations in its Jurisdictional Statement which have never been presented before. In its Stay filed on September 22, 1981, to this U. S. Supreme Court, CEI argued that if it could not include the amortization for the terminated plants, its rate of return "must be below" the rate of return authorized by the PUCO, and thus its property was being confiscated. The Senior Citizens Coalition, et al, in its Memorandum filed October 7, 1981, in opposition to this Stay, pointed out the fallacy of such an argument. The mere difference between a rate of return with the amortization as opposed to one without amortization does not necessarily show confiscation. On page 18 and 19 of its Jurisdictional Statement, CEI tries to patch up this hole in its case by performing calculations and referring to documents, such as its 1980 Annual Statement, which were never part of this case. Furthermore, how are the Appellees ever going to be able to cross-examine whoever is presenting such evidence if indeed the names of the Unknown Calculators are ever revealed.

explore these because CEI's appeal should and must be dismissed. The federal questions the Appellant seeks to have reviewed were neither timely nor properly raised nor were these questions expressly passed upon within Ohio's judicial system.

United States Supreme Court Rule 16 (1)(b) states, "The Court will receive a motion to dismiss an appeal from a state court on the ground....that the federal question sought to be reviewed was not timely or properly raised and was not expressly passed on...." The position of the Senior Citizens Coalition, et al, is that both conditions for this ground of dismissal are satisfied in this case.(3)

---

(3) CEI's appeal is also subject to dismissal based upon another ground in Rule 16(1)(b) because the Ohio Supreme Court's decision rests on an adequate non-federal basis. The Court's decision was strictly limited to construing Ohio's ratemaking formula.

First, the Appellant failed to raise timely and properly its alleged federal questions. This can be analyzed in terms of (1) when did the Appellant raise its federal questions and (2) when should it have raised these questions.

Appellant claims that it "alerted" the Ohio Supreme Court in its first brief about "the constitutional problem." (See page 10 of CEI's Jurisdictional Statement.) Yet a review of the Proposition of Law and its sub-parts presented by the Appellant CEI in its Brief nowhere even alludes to any Federal Constitutional dimension for why the amortization of the four terminated plants must be allowed.(4)

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(4) This is CEI's Proposition of Law and its subparts presented to the Ohio Supreme Court before the oral hearing and decision:

PROPOSITION OF LAW NO. 1
THE PUBLIC UTILITIES COMMISSION ACTED REASONABLY AND LAWFULLY

Footnote No. 4 continued:

IN RECOGNIZING, AS AN ALLOWABLE EXPENSE FOR RATE MAKING PURPOSES, AN AMORTIZED PORTION OF EXPENDITURES PRUDENTLY INCURRED FOR THE PROVISION OF ELECTRIC SERVICE.

1. In Deciding This Issue The Commission Met All Ohio Procedural Requirements.

2. There Is No Question But That The Ohio Statutory Framework Permits Recognition Of The Expenses Here In Question For Rate Making Purposes.

3. On The Record In This Proceeding, The Commission's Decision To Include An Amortization Of The Expenses In Question Was Reasonable.

4. The Decision Of The Public Utilities Commission Of Ohio To Allow The Termination Costs Amortized Over Ten Years Is Consistent With The Decisions Of Other Jurisdictions.

Certainly the majority decision of the Ohio Supreme Court delivered by Justice Sweeney nowhere indicates that CEI had "alerted" the court that it was claiming any Constitutional rights. Even more telling is the fact that the minority opinion, written by Justice Brown who favors the PUCO's decision, never mentions any Constitutional rights or federal questions.

The first time when CEI explicitly contends for alleged rights under the Fifth and Fourteenth Amendments occurs in its Motion for Rehearing. (See pages 11 and 12 of CEI's Jurisdictional Statement.) The question of whether this was timely and properly done is itself, of course, a federal question. See Street v. New York, 394 U.S. 576 at 583, 89 S. Ct. 1354 at 1361 (1969). The answer to such a question does, however, demand an examination of

State procedures. No particular formula or set phrases are needed to challenge the validity of a State law, only that "the ground therefor be brought to the attention of the state court with fair precision and in due time." (Emphasis supplied, New York ex rel. Bryant v. Zimmerman, 278 U.S. 63 at 67, 49 S. Ct. 61 at 63 (1928).

There is no doubt that CEI could have explicitly raised its federal questions and constitutional rights at a much earlier point in the entire proceeding. The very decision cited by Appellant CEI from the Virginia utilities commission including the quotation from the dissenting Commissioner Shannon suggests that CEI could have argued its Constitutional claims during the PUCO proceedings prior to any court appeal. (See page 11 of CEI Jurisdictional Statement.) In

fact, the PUCO has allowed this. During the last CEI general rate case, In Re Cleveland Electric Illuminating Company, PUCO 80-376-EL-AIR, the PUCO considered and rejected Federal Constitutional issues asserted by the Senior Citizens Coalition, et al, while the hearings were still in progress before the Hearing Examiner. (See paragraph 6 of Entry dated March 11, 1981.)

Certainly, when CEI submitted its Brief to the Ohio Supreme Court opposing the appeal of the Senior Citizens Coalition, et al, as well as the appeals of the Ohio Consumers Counsel and the City of Cleveland, the Company could have asserted its claimed Constitutional rights. The Supreme Court Rules of Practice for Ohio support the proposition that CEI was required to assert such alleged rights in this Brief. Ohio Supreme Court Rule V, Section 2,

entitled "Brief Opposing Appeal,"

declares:

> Within thirty days of the filing of appellant's brief, the party opposing the appeal shall file a brief complying with the provisions of this rule and Rule VI and answering the appellant's contentions and making any other contentions deemed appropriate as reasons for affirmance of the order or judgment appealed from.

The very Constitutional rights which the Appellant only raised expressly in its Motion for Rehearing would seem to be "any other contentions" which appellant should have raised in its initial brief before the oral hearing and decision. This conclusion is further supported by Section 1(D) of Ohio Supreme Court Rule V which required the Senior Citizens, brief to contain--and thus CEI's brief by operation of Section 2--"an argument, which shall be headed by the proposition of law which

the appellant contends is applicable to the facts in the case and which, if he prevails, could serve as a syllabus." CEI's proposition of law and its sub-parts on the four cancelled nuclear plants, which have already been quoted, contained nothing about federal questions or alleged Constitutional rights.

This statutory argument that CEI raised its alleged constitutional arguments too late has also a rational and logical basis for support. By raising constitutional arguments as early as possible, a party places all other parties as well as each decision-making institution on notice about its claims. A more adequate record can be compiled with the proper presentation and cross-examination of evidence relative to constitutional claims. This also insures more

thorough consideration of these claims by administrative bodies and courts. In our Federal system, it is especially important that a State's courts at least have an adequate opportunity to interpret its laws in light of any claims of constitutional challenge, especially when such important statutory schemes as utility regulation which impact more and more upon every citizen, business and insustry of that state are at stake. See Cardinale v. Louisiana, 394 U.S. 437 at 439, 89 S. Ct. 1161 at 1163 (1969).

In this particular case, CEI explicitly raised its federal questions virtually after the case was over. CEI's arguments in its rehearing came after the evidentiary hearings before the PUCO hearing examiner, after the briefs and reply briefs of all parties for the PUCO, after the PUCO Opinion

and Order, after the request to the PUCO for a rehearing, after the Notice of Appeal to the Ohio Supreme Court, after the briefs were submitted by CEI and the other parties for the Ohio Supreme Court, after the oral argument before all the Justices of the Ohio Supreme Court, after the deliberations of that Court, and after the decision of the Ohio Supreme Court. This hardly seems like adequate and timely notice, especially given the seeming importance CEI attaches to this issue and the public outcry before the PUCO against charging customers for plants that will never serve them. Based on the procedures governing appeals to the Ohio Supreme Court as well as reason and logic, it was improper for CEI to wait until a Motion for Rehearing before raising such contentions.

Second, the federal questions now raised by the Appellant must have been "expressly passed on" by the state court in order for this Court to assume jurisdiction. The Ohio Supreme Court's decision, including the dissenting opinion, never even mentions any federal question. Since that court rendered no written opinion in rejecting CEI's Motion for Rehearing, there is again nothing expressly passing upon the questions raised by the Appellant.

The Senior Citizens Coalition, et al, however, do acknowledge that an inquiry is necessary to determine if the Ohio Supreme Court in rejecting CEI's Motion for Rehearing may have necessarily decided on the validity of CEI's constitutional claims. See Crowell v. Randell, 10 P. 368 at 391-2, 12 Curtis 164 at 165-6 (1836). CEI in its Jurisdictional Statement overlooks this

issue and blandly asserts, "The Supreme Court of Ohio denied appellant's Motion for Rehearing, thereby deciding in favor of [constitutional] validity of those statutes, as so construed." (See page 10 of CEI's Jurisdictional Statement.) The Appellant cites no cases and offers no legal or rational analysis for this naked conclusion.

This U.S. Supreme Court itself may reject a party's attempt to raise a Constitutional issue without necessarily deciding the merits of that issue. For example, this Court has refused to consider an alleged violation of Constitutional rights when such a claim was never made in the party's Jurisdictional Statement. Quilloin v. Walcott, 434 U.S. 246, 98 S. Ct. 549 (1978), rehearing denied 435 U.S. 918, 98 S. Ct. 1477 (1978). U. S. Supreme Court Rule 16(1)(b) also embodies the

idea that constitutional claims can be rejected--without ruling on their merits--when such claims have not been properly raised. Similarly, it may not be either unreasonable or improper for Ohio's Supreme Court to reject CEI's Motion for Rehearing even when CEI tries to raise Constitutional claims without the Court expressly ruling on those claims.

Indeed an analysis of the procedures and rationale of the Motion for Rehearing under Ohio Law not only fails to support CEI's naked assertion, but leads to the opposite conclusion. Very early in Ohio legal history, following the lead of the U. S. Supreme Court in Brown v. Aspden, 14 How 25 (1852), the Ohio Supreme Court decided that there was no "right of the parties to compel us to reinvestigate the merits of a controversy once determined by the petition for

rehearing...." Longworth & Horne v. Sturges & Anderson, 2 Ohio St. 105 (1853) at 107-8. The wise use of scarce judicial resources as well as fairness to other parties--and even fairness to those involved in other cases who are pursuing their own appeals and a speedy resolution of their own controversies--impel such a result. The contrary practice could lead to the endless re-arguing of cases, both to the detriment of those involved as well as of others standing in line to have their rights determined.

The current Rule IX of the Ohio Supreme Court Rules of Practice embodies this ideal of fairness and due process in Section 1 when it states, "Such motion [for rehearing] must be confined strictly to the grounds urged for rehearing and must not constitute a reargument of the case." When CEI

refashions its arguments, only now clothed in Constitutional garb, it is merely rearguing its case.

While there is some authority in Ohio that an appellate court can in a rehearing examine questions and propositions of law which have not been given attention, there is no requirement. (See discussion in "Appellate Review, Section 510, 5 O. Jur. 3d (1978).) A rehearing is not meant as a way of invoking an expression from the court upon matters which have already been carefully and thoroughly explored.

The propositions of law that the Appellant offers in its Motion for Rehearing are matters which could and should have been asserted much earlier. While a Rehearing might be appropriate to bring up some new questions or propositions of law, especially where these could never have been anticipated

in the original appeal, it hardly seems like the proper time in this case to assert alleged constitutional arguments of which CEI by its own admission was well aware when it originally submitted its brief to the Ohio Supreme Court. (See pages 10-1 of CEI's Jurisdictional Statement.)

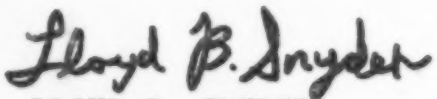
In summary, the Appellant cannot point to anything which shows that the federal questions it now raises in its Jurisdictional Statement were "expressly passed on" by the Ohio Supreme Court or the PUCO. The Court's mere denial of CEI's Motion for Rehearing does not necessarily imply that the Ohio Supreme Court passed upon these asserted federal questions, but rather seems like a wise discretionary decision protective of the Court's processes which insure due process to all parties. (See

Edelman v. People of State of Cal., 344 U.S. 357, 73 S. Ct. 293 (1953); Spies v. Illinois, 123 U.S. 131, 8 S. Ct. 21 (1887); St. Louis and San Francisco Railroad v. Shepherd, 240 U.S. 240, 36 S. Ct. 274 (1916); and McMillen v. Ferrum Mining Company, 197 U.S. 343, 25 S. Ct. 533 (1905).

CONCLUSION

In its Jurisdictional Statement, CEI has sought to raise two federal questions. Neither of these questions was timely or properly presented by CEI either to the PUCO or the Ohio Supreme Court. Moreover, neither federal question was expressly passed upon. Therefore, the Senior Citizens Coalition, the Greater Cleveland Welfare Rights Organization, Inc., Western Reserve Alliance, North Shore Alert, and the Cleveland Chapter of Ohioans for Utility Reform respect-

fully move this Honorable Court to grant their Motion and dismiss this appeal.(5)



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(5) All of the Appellees are well aware that there are cases pending in other jurisdictions on similar issues of how to handle costs relating to the cancellation of large utility generating plants. Yet these other cases should not be used to rush the United States Supreme Court into making a decision on any alleged federal questions. Indeed it may be more just to the other utility companies as well as insuring regard for our Federal system with its careful balance of Federal and State

Footnote No. (5) continued:

interests to await a case where any alleged constitutional issues have been more adequately considered in the state proceeding. For these reasons as well as for the others already presented in this Brief, the Senior Citizens Coalition, et al, would also urge this Court not to grant any writ of certiorari in this case. (See page 1 of CEI's Jurisdictional Statement.)

APPENDIX

STATUTES AND REGULATIONS INVOLVED

1. Ohio Supreme Court Rule V, Section 1, Appellant's Brief, states in pertinent part as follows:

> "The appellant's brief must comply with Rule VI and contain:
>
> (A) A table of contents listing the table of authorities, statement of facts, argument (with the proposition or propositions of law and authorities relied upon to support the same) ..."
>
> "(D) An argument, which shall be headed by the proposition of law which the appellant contends is applicable to the facts in the case and which, if he prevails, could serve as a syllabus."

2. Ohio Supreme Court Rule V, Section 2, Brief Opposing Appeal, states in pertinent part as follows:

> Within thirty days of the filing of appellant's brief, the party opposing the appeal shall file a brief in form complying with the provisions of this rule and Rule VI and answering the appellant's contentions and making any other contentions deemed appropriate as reasons for affirmance of the order or judgment appealed from.

3. Ohio Supreme Court Rule IX, Section 1, Motion for Rehearing, states as follows:

> A motion for rehearing shall be filed within ten days after the announcement of the decision. Such motion must be confined strictly to the grounds urged for rehearing and must not constitute a reargument of the case. Notice of such motion shall be served on opposing counsel who shall have five days to file his memorandum contra.

4. Ohio Revised Code Section 4909.15 - Fixation of Rates by Commission - states in pertinent part as follows:

> **4909.15 Fixing of reasonable rate**
>
> (A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:
>
> (1) The valuation as of the date certain of the property of the public utility used and useful in rendering the public utility service for which rates are to be fixed and determined. The valuation so determined shall be the total value as set forth in division (J) of section 4909.05 of the Revised Code, and a reasonable allowance for materials and supplies and cash working capital, as determined by the public utilities commission. The commission may, in its discretion, permit a reasonable allowance for construction work in progress but, in no event, may any allowance for construction work in progress be made by the commission until it has determined, after a physical inspection, that the particular construction project is at least seventy-five per cent complete.
>
> (2) A fair and reasonable rate of return to the utility

on the valuation as determined in division (A)(1) of this section;

(3) The dollar annual return to which the utility is entitled by applying the fair and reasonable rate of return as determined under division (A)(2) of this section to the valuation of the utility determined under division (A)(1) of this section;

(4) The cost to the utility of rendering the public utility service for the test period less the total of any interest on cash or credit refunds paid, pursuant to section 4909.42 of the Revised Code, by the utility during the test period. Federal, state, and local taxes imposed on or measured by net income may, in the discretion of the commission, be computed by the normalization method of accounting, provided the utility maintains accounting reserves that reflect differences between taxes actually payable and taxes on a normalized basis. provided that no determination as to the treatment in the rate making process of such taxes shall be made that will result in loss of any tax depreciation or other tax benefit to which the utility would otherwise be entitled, and further provided that such tax benefit as redounds to the utility as a result of such a computation may not be retained by the company, used to fund any dividend, or utilized for any purpose other than the defrayal of the operating expenses of the utility and the defrayal of the expenses of the utility in connection with construction work.

(B) The public utilities commission shall compute the gross annual revenues to which the utility is entitled by adding the dollar amount of return under division (A)(3) of this section to the cost of rendering the public utility service for the test period under division (A)(4) of this section.

(C) The test period, unless otherwise ordered by the public utilities commission, shall be the twelve-month period beginning six months prior to the date the application is filed and ending six months subsequent to that date. The revenues and expenses of the utility shall be determined during the test period. The date certain shall be not later than the date of filing.

(D) When the public utilities commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section, that any rate, fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is, or will be, unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law,

that the service is, or will be, inadequate, or that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

(1) With due regard among other things, to the value of all property of the public utility actually used and useful for the convenience of the public as determined under division (A)(1) of this section, excluding from such value the value of any franchise or right to own, operate, or enjoy the same in excess of the amount, exclusive of any tax or annual charge, actually paid to any political subdivision of the state or county, as the consideration for the grant of such franchise or right, and excluding any value added to such property by reason of a monopoly or merger, with due regard in determining the dollar annual return under division (A)(3) of this section to the necessity of making reservation out of the income for surplus, depreciation, and contingencies, and;

(2) With due regard to all such other matters as are proper, according to the facts in each case,

(a) Including a fair and reasonable rate of return determined by the commission with reference to a cost of debt equal to the actual embedded cost of debt of such public utility,

(b) But not including the portion of any periodic rental or use payments representing that cost of property which is included in the valuation report under divisions (F) and (G) of section 4909.05 of the Revised Code, fix and determine the just and reasonable rate, fare, charge, toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one. After such determination and order no change in the rate, fare, toll, charge, rental, schedule, classification, or service, shall be made, rendered, charged, demanded, exacted, or changed by such public utility without the order of the commission, and any other rate, fare, toll, charge, rental, classification, or service is prohibited.

(E) Upon application of any person or any public utility, and after notice to the parties in interest and opportunity to be heard as provided in Chapters 4901., 4903., 4905., 4907., 4909., 4921., and 4923. of the Revised Code for other hearings, has been given, the commission may rescind, alter, or amend an order fixing any rate, fare, toll, charge, rental, classification, or service, or any

other order made by the commission. Certified copies of such orders shall be served and take effect as provided for original orders.

In no event shall an allowance for construction work in progress under division (A)(1) of this section exceed twenty per cent of the total valuation as stated in such division, not including such allowance.

Motion to Dismiss or Affirm

3

Office-Supreme Court, U.S.
FILED
DEC 28 1981
ALEXANDER L. STEVAS,
CLERK

CASE NO. 81-1002

In The

SUPREME COURT OF THE UNITED STATES

October Term, 1981

The Cleveland Electric Illuminating Company,
Appellant,

vs.

Office of the Consumers' Counsel
Senior Citizens Coalition, et al.
City of Cleveland

and

The Public Utilities Commission of Ohio,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF OHIO

MOTION OF APPELLEE, OFFICE OF THE CONSUMERS' COUNSEL, TO DISMISS APPEAL, OR IN THE ALTERNATIVE, MOTION TO AFFIRM

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TABLE OF CONTENTS

Page

Table of Authorities ii

Statement of the Case 1

Motion to Dismiss or in the Alternative to Affirm 5

Argument in Support of Motion to Dismiss 5

Argument in Support of Motion to Affirm 17

Conclusion 24

TABLE OF AUTHORITIES

Cases

Page

Bluefield Water Works Co. v. Public Service Commission, 262 U.S. 679 (1923) 18, 19, 22

C&SOE v. Pub. Util. Comm., 64 Ohio St.2d 175, 407 N.E.2d 23 (1980) 16

Cleveland v. Pub. Util. Comm., 164 Ohio St. 442, 132 N.E.2d 216 (1956) 14

Cleveland v. Pub. Util. Comm., 63 Ohio St. 2d 62 (1980) 15

Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d 153, 423 N.E.2d 820 (1981) 4, 17, 19, 23

Durley v. Mayo, 351 U.S. 277 (1956) 21

East Ohio Gas Company v. Pub. Util. Comm., 133 Ohio St. 212, 12 N.E.2d 765 (1938) 14

Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944) 17, 20, 22

Garner v. Louisiana, 368 U.S. 157 (1961) 18, 20

Henry v. Mississippi, 379 U.S. 443 (1965) 21

Kulko v. Superior Court of California, 436 U.S. 84 (1978) 6

NEPCO Municipal Rate Committee v. Federal Energy Regulatory Commission, Case No. 80-1343 (D.C. Cir., Oct. 15, 1981) 19

New York ex rel. Bryant v. Zimmerman, 278 U.S. 63 (1928) 8

Pacific Gas & Electric Co. v. San Francisco, 265 U.S. 403 (1924) 19

Saunders v. Shaw, et. al., 244 U.S. 317 (1917) 12

Slade v. Ohio, 366 U.S. 259 (1961) 7

State of Missouri ex rel. Missouri Insurance Co. v. Gehner, 281 U.S. 313 (1930) 12, 13

Webb v. Webb, _____ U.S. _____, 101 S. Ct. 1889 (1981) 8, 9, 10, 16

Younger v. Harris, 401 U.S. 37, 44 (1971) 9

Zacchini v. Scripps Howard Broadcasting Co., 433 U.S. 562 (1977) 21

Statutes

28 U.S.C. §1257 (2) 5, 6, 7

Ohio Rev. Code §4909.15 (A) (4) 2, 13, 14, 17, 20

Ohio Rev. Code §4905.22 .....1, 14, 15, 17

STATEMENT OF THE CASE

Appellee, the Office of Consumers' Counsel, will confine its statement of the case to those points with which it disagrees with the Appellant's Statement of the Case in Appellant's statement in support of jurisdiction. The procedural aspects of this case with respect to the course of proceedings below, as set forth in Appellant's Jurisdictional Statement, are correct except as noted hereafter.

Appellant correctly notes that the source of the present controversy is a decision of the Ohio Supreme Court, dated July 15, 1981. That decision reversed a finding by the Ohio Public Utilities Commission that Appellant's rates for rendering its public utility service be based in part on the amortization of costs associated with the planning, engineering and preliminary construction costs related to the construction of four nuclear generating units. The construction of those units was terminated on January 23, 1980.

On July 15, 1981, the Ohio Supreme Court, in a 5-2 decision reversed this finding by the Public Utilities Commission of Ohio. The decision of the Ohio Supreme Court was simply one of statutory interpretation, regarding the Ohio statute which sets forth the manner in which rates for Ohio public utilities are to be determined by the Public Utilities Commission. Contrary to the assertions in Appellant's statement of the case, the Ohio Supreme Court did not reject the provisions of the Uniform System of Accounts prescribed for electric utilities, nor did it agree that Ohio Rev. Code §4905.22 required appellant to invest the capital

associated with the cancelled nuclear generating units in that project. Moreover, the Ohio Supreme Court did not *reject* the overwhelming weight of authority from other jurisdictions in rendering its decision, but noted that none of the decisions from those other jurisdictions represented the opinion of the highest court in the jurisdiction wherein each of those cases arose, that none of those cases considered the propriety of the Ohio Commission's actions with reference to Ohio law, and that *the construction of Ohio law is particularly the province of the Ohio Supreme Court.* Finally, the Ohio court never agreed that the expenditures by the Appellant for the terminated nuclear units were prudent, for it was not required to reach that issue in order to decide the case. Thus, the entire factual background presented by Appellant with respect to the planning and initial construction of the generating units is irrelevant to the determination of the issues arising from this proceeding and need not be addressed by Appellee.

In the proceeding below, the Ohio Supreme Court was faced with the necessity of determining whether the costs associated with the terminated nuclear units were a proper cost of service upon which the utility's rates could be based. At question was Ohio Rev. Code §4909.15 (A) (4), which statute governs ratemaking in Ohio. The crux of the controversy in this case is best stated in the words of the Ohio Supreme Court:

> The controversy surrounding the cancelled nuclear power plants focuses primarily on R. C. 4909.15 (A) (4), which delineates the service-related costs that a utility may recover from

its ratepayers. This section states in relevant part:

"The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges shall determine:

"***

"(4) The cost to the utility of rendering the public utility service for the test period***."

The commission urges that "an expenditure by a utility can be considered a cost of rendering the public utility service if it fails in fact to achieve its intended purpose*** [if] the expense was reasonably calculated to provide [future] utility service at a reasonable cost." The underpinnings for the commission rationale may be found in those statutory provisions that require utilities to maintain adequate service presently and for the foreseeable future. See, *e.g.*, R. C. 4905.22 (adequate service and facilities).

Notwithstanding the provisions that impose a duty on utility companies to plan for the future, the question under R. C. 4909.15 (A) (4) remains whether the cancelled plant expenditures represent "[t]he cost to the utility of rendering the public utility service for the test period." Test period considerations aside, what the company sought and what the commission granted was the amortization as service-related costs of an investment that never provided any service whatsoever to the utility's customers.

We seriously question whether the General Assembly contemplated that the commission would treat the type of expenditures controverted herein as costs under R. C. 4909.15 (A) (4). The now terminated nuclear plants rep-

resented a major capital investment that ultimately would have been included in the rate base under R. C. 4909.15 (A) (1), had the projects not been cancelled. It is our opinion that R. C. 4909.15 (A) (4) is designed to take into account the normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period.[8] A nonexhaustive list of such expenses would include reasonable expenditures for repairs, maintenance, personnel-related costs, administrative expenses, and taxes.

The extraordinary loss sustained by CEI in connection with the terminated nuclear plants cannot be transformed into an ordinary operating expense pursuant to R. C. 4909.15 (A) (4) by commission fiat. The commission's statement that "[c]ancellation does not create a past loss, but gives rise to a current cost" is unpersuasive. Under this rationale we question whether there could ever be a "past loss" the return of which would not be recoverable in future ratemaking proceedings notwithstanding the commission's assertion to the contrary. The commission's characterization of the investment in the four terminated plants as "cost" under R. C. 4909.15 (A) (4) in light of what we perceive to be the legislative intention underlying that section is unreasonable. Therefore, to the extent that the commission's order in regard to the cancelled plants is predicated on R. C. 4909.15 (A) (4), the order cannot stand.

Consumers' Counsel v. Pub. Util. Comm., 67 Ohio St.2d 153, 423 N.E.2d 820 (1981)

This excerpt from the court's opinion clearly demonstrates the limited scope of the issue on appeal.

The Appellant did not alert the Ohio Supreme Court to the constitutional arguments it now pur-

sues in this appeal. Thus, the Ohio Supreme Court was not presented with any constitutional issues, nor, *a fortiorari*, did the Ohio Supreme Court expressly pass upon any constitutional questions or affirm the validity of the ratemaking statute here in question.

MOTION TO DISMISS AND IN THE ALTERNATIVE, MOTION TO AFFIRM

Pursuant to Supreme Court Rule 16.1(b), the Appellee, Office of the Consumers' Counsel, hereby moves that this Court dismiss the Appeal of the Cleveland Electric Illuminating Company as improperly taken from the Supreme Court of Ohio under 28 U.S.C. 1257(2). In the alternative, the Office of the Consumers' Counsel moves that this Court affirm the decision of the Supreme Court of Ohio rendered in the case below.

ARGUMENT IN SUPPORT OF MOTION TO DISMISS

The Appellant has invoked the jurisdiction of this Court under 28 U.S.C. §1257(2). which states in pertinent part:

> Final judgments or decrees rendered by the highest court of a state in which a decision could be had, may be reviewed by the Supreme Court as follows:
>
> * * * *
>
> (2) By appeal, where is drawn in question the validity of a statute of any state on the ground of its being repugnant to the Constitution, treaties or laws of the United States, and the decision is in favor of its validity.
>
> * * * *

The express language of 28 U.S.C. §1257(2) requires that the highest court of a state render a decision favoring the validity of a state statute before review of the state court decision may be sought in the Supreme Court of the United States. The necessary predicate of an appeal under 28 U.S.C. §1257(2) is, therefore, that the validity of the state statute in question must first be challenged in the state court. Where the highest court of a state is not called upon to review a statute claimed to be in conflict with the United States Constitution, or where that state court renders a decision which does not address the validity of the statute, an appeal under 28 U.S.C. §1257(2) will not lie. *Kulko v. Superior Court of California*, 436 U.S. 84 (1978).

In the present case the appellant failed to draw in question the validity of an Ohio statute in the proceedings before the Ohio Supreme Court, such that the Ohio Supreme Court could decide upon the constitutional validity of the Ohio statute. Review of the opinion of the Ohio Supreme Court reveals that nowhere is any federal question mentioned, let alone expressly passed upon. Nor is any federal question mentioned in the dissenting opinions in that decision. Review of Appellant's Brief filed with the Ohio Supreme Court reveals that Appellant devoted pages 8 through 31 of that Brief to the question of recovery of expenses associated with cancelled nuclear plants. The word "constitutional" is mentioned but once, at page 21. Even then, the word appears in part of a quotation from a dissenting opinion in a matter before the

Virginia State Corporation Commission.* It is puzzling, therefore, that Appellant can assert at page 10 of its Jurisdictional Statement that:

> CEI alerted the Ohio Supreme Court in its first brief in this case of the constitutional problem which might arise if the Ohio ratemaking formula were construed to prohibit recovery of necessary and prudent planning costs in some fashion.

Indeed, there is no mystery surrounding Appellant's failure in its jurisdictional statement to cite this Court to the pages in its Brief filed with Ohio Supreme Court wherein it argued that denial of recovery of the nuclear plant expenses would constitute an unconstitutional taking of its property. It could not do so for it never presented the issue to the Ohio Supreme Court before rehearing. The Ohio Supreme Court, not having been presented with a federal question before it decided the case could therefore not have expressly passed upon that question.

In circumstances such as these, it is clear that an appeal to this Court under 28 U.S.C. §1257(2) will not lie. The burden of proving the timely presentation of a federal question in a state court is on the party seeking appellate review. *Slade v. Ohio*, 366 U.S. 259, 264 (1961). The United States Supreme Court has often stated that when "the highest state court has failed to pass upon a federal ques-

---

*Moreover, the Appellant's use of the quotation is presented, *not* to urge that disallowance of the costs would be unconstitutional, but rather to support the premise that the Ohio commission should somehow have afforded the subject expenses with the treatment advocated in the dissent.

tion, it will be assumed that the omission was due to want of proper presentation in the state courts, unless the aggrieved party in this Court can affirmatively show the contrary," *Webb v. Webb*, ___ U.S. _____, 101 S.Ct. 1889, 1891 (1981) (citing *Street v. New York*, 394 U.S. 576 (1969) and other cases). Furthermore, the jurisdiction of the United States Supreme Court to review decisions of state courts can arise only if the record as a whole shows, either expressly or by clear implication, that the federal question was adequately presented to the state court. *Webb v. Webb*, ___ U.S. _____, 101 S.Ct. 1889, 1892 (1981); *New York ex rel. Bryant v. Zimmerman*, 278 U.S. 63 (1928).

Although it was brought to this Court on petition for a writ of certiorari, the *Webb* case, *supra*, contains an excellent discussion of the considerations which underlie this Court's consistent refusal to decide federal constitutional questions raised for the first time on appeal to this Court. In the opinion delivered by Mr. Justice White, this Court held that:

> [t]here are powerful policy considerations underlying the statutory requirement and our own rule that the federal challenge to a state statute or other official act be presented first to the state courts. These considerations strongly indicate that we should apply this general principle with sufficient rigor to make reasonably certain that we entertain cases from state courts *only where the record clearly shows that the federal issue has been properly raised below.*
>
> *Webb, supra*, ___ U.S. _____, 101 S.Ct 1889, 1893 (1981) (Emphasis added).

The policy reasons supporting the Court's reluctance to hear cases brought before it from state

courts are found first in the principles of comity in the federal system. The comity principle requires that state courts be given an opportunity to perform their duty, which includes deciding questions of the validity of state statutes under attack on constitutional grounds. This Court noted that the principle of comity requires:

> a proper respect for state functions, a recognition of the fact that the entire country is made up of a Union of separate state governments, and a continuance of the belief that the National Government will fare best if the states and their institutions are left free to perform their own separate functions in their separate ways.
>
> *Younger v. Harris*, 401 U.S. 37, 44 (1971).

In addition to this policy reason, practical reasons abound for this Court's insistence that federal questions be first presented in the state courts. First, such a requirement affords the parties to litigation "an opportunity to develop the record necessary for adjudicating the issue." *Webb, supra*, ___ U.S. _____, 101 S.Ct. 1889, 1893 (1981). Second, it allows the state court to exercise its authority to construe state statues so as to obviate federal constitutional challenges. *Id.* at 1893-94. Furthermore, the rule allows state courts to identify and act upon independent, adequate state grounds which will pretermit federal issues. *Id.* Last:

> if the parties to state court litigation are required to present their federal claims in state tribunals in the first instance, those issues will be adjudicated in the state courts where necessary to dispose of the case. In most instances, such a judgment will be supported by an opinion that may well obviate any reason

> for our giving plenary consideration to the case. In terms of our own workload this is a very substantial matter.
>
> *Id.*, at 1894.

Thus has this Court stated the bases for its policy against acceptance of plenary jurisdiction unless the appellant has first raised the federal question in the state Court and had that federal question expressly ruled upon. As this Court also noted:

> At the minimum, however, there should be no doubt from the record that a claim under a *federal* statute or the *Federal* constitution was presented in the state courts and that those courts were apprised of the nature or substance of the federal claim at the time and in the manner required by state law. Otherwise, we cannot be sufficiently sure, when the state court whose judgment is being reviewed has not addressed the federal question that is later presented here, that the issue was actually presented and silently resolved by the state court against the petitioner or the appellant in this Court.
>
> *Id.*

The matter *sub judice* is one in which the Court should apply the foregoing standards of review and refuse to accept jurisdiction. Appellant *never* apprised the Ohio Supreme Court of the possibility of there being a federal question in this case. Not until after the Ohio Supreme Court issued its decision on July 15, 1981, did Appellant belatedly attempt to interject the Constitutional arguments it asserts before this Court. Only in its Motion for Rehearing did Appellant raise a Federal constitutional question. The Appellant clearly had the opportunity and right, if it wished, to present the

Ohio Supreme Court with its Federal constitutional arguments at a point in time when the record could have been developed to properly adjudicate this issue. The Appellant chose not to do so. The Ohio Supreme Court, had Appellant properly raised its constitutional arguments, could have exercised its authority to construe the state statute here in question so as to obviate the need for a federal constitutional challenge. It did not, indeed could not, expressly pass upon the validity of the statute as interpreted by it because Appellant never timely presented its constitutional arguments. Indeed, the Ohio Supreme Court overruled Appellant's Motion for Rehearing without comment, thus not expressly passing upon the federal question.

Appellant's argument, it seems, is somewhat unclear even to Appellant. On the one hand, Appellant has asserted that it alerted the Ohio Supreme Court of the constitutional problem which might arise if that court construed the Ohio statue so as to prohibit recovery of the expenses of the cancelled plants. If we assume, *arguendo*, that this is true, then on what grounds may Appellant claim surprise by the Ohio Supreme Court's decision? Had Appellant in actuality raised its constitutional arguments on a timely basis before the Ohio Supreme Court, that court would have been presented the opportunity to address this issue, and Appellant should not therefore be heard to complain about the Ohio Supreme Court's decision.

Appellee suspects that Appellant will ask this Court to grant plenary jurisdiction, based on two decisions by this Court allowing review in cases in which the constitutional challenges were first raised on petitions for rehearing *after* issuance of decisions by the highest court of the subject states.

Both cases represent an exception to the rule that the United States Supreme Court will not ordinarily "consider contentions first made in a petition to the state court for rehearing where the petition is denied without more." *State of Missouri ex rel. Missouri Insurance Co. v. Gehner*, 281 U.S. 313, 320, (1930) (hereinafter referred to as *Gehner*). The first of these cases is *Gehner, supra*. The second is *Saunders v. Shaw, et al.*, 244 U.S. 317 (1917) (hereinafter referred to as *Saunders*).

Both cases are clearly distinguishable from the matter *sub judice*. In *Saunders*, the trial court issued a decision favoring the defendant. During the trial, the lower court ruled certain of plantiff's evidence inadmissable, and thereafter certain of defendant's evidence, which would have contradicted plaintiff's evidence, was not allowed into the record, the question not being open. The trial court issued a verdict for defendant, and the state supreme court initially affirmed. On rehearing, however, the state supreme court reversed, issuing a decision on the merits for plaintiff without ever letting defendant introduce the evidence favorable to him. Thereafter, the defendant petitioned for certiorari to the United States Supreme Court, because a state supreme court rule provided for only one rehearing. Thus, defendant's *only* available means to assert his right to due process of law was by appeal to the United States Supreme Court. In *Gehner, supra*, the appellant, *at the first opportunity*, invoked the protection of the federal constitution, and that first opportunity was after issuance of a decision by the state supreme court. This Court held that the appellant was not bound to anticipate the eventual construction placed on a statute by the state supreme court and stated that:

> *Upon the facts disclosed by this record* it is clear that appellant sufficiently raised in the highest court of the state the Federal questions here presented and is entitled to have them considered.

Gehner, 281 U.S. 313, 320 (1930) (Emphasis added.)

Both cases clearly turn on the fact that the appellants could not have raised their constitutional arguments earlier than they did. In this matter, however, such is not the case.

Appellant in this case asserts that it, in its very first Brief, alerted the Ohio Supreme Court to its constitutional questions. Thus we *must* assume that it was aware, before it filed its initial brief, of the potential for an unconstitutional taking of its property if the Ohio Supreme Court reversed. If it was so aware, why did it not elaborate on Brief and allow the Ohio Supreme Court the opportunity to decide the issue? The reasons for this failure must remain conjecture.

More importantly, however, the appellant cannot claim surprise at the state court's decision construing the statute in question unfavorably for the appellant.

It may be true, as Appellant claims, that in its decision the Ohio court construed "cost" for the first time in Ohio Rev. Code §4909.15(A) (4) to exclude from allowable expenses the costs associated with cancelled generating plants, but only because it is the first time the court considered these specific costs. It is not true, however, that this is the first time that allowable costs were excluded because they were unrelated to the actual rendition of service or because they were non-

recurring past losses. Furthermore, it is a misrepresentation that this is the first time that costs incurred by a utility to fulfill its statutory duty under Ohio Rev. Code §4905.22 to provide adequate service have been disallowed.

More than forty years ago, the Ohio court established a standard which cannot be interpreted to permit expenses not related to the actual rendition of service:

> Operating expenses are to be based upon the management of property which is used and useful.
>
> *East Ohio Gas v. Pub. Util, Comm.*, 133 Ohio St. 212, 233 (1938).

Twenty-five years ago, the Ohio Supreme Court delineated six criteria for ratemaking, the fourth of which clearly joined the determination of allowable expenses to the rendition of service:

> 4. Determine the dollar amount of *the cost of rendering the public utility service* for a particular year. This dollar amount shall be referred to herein as annual expenses.
>
> *Cleveland v. Pub. Util. Comm.*, 164 Ohio St. 442, 443-444 (1966) (Emphasis added.)

Only last year, the Ohio court, noting that the Commission's authority to permit recovery of operating expenses is found in Ohio Rev. Code §4909.15 (A) (4), reviewed the propriety of certain expenses on the precise rendition of service standard applied herein (this proceeding involved the rates of Appellant):

> Our task upon review is to determine whether appellee could reasonably and lawfully con-

> clude that the instant expenses were related to *the cost of rendering the public utility service.*
>
> *Cleveland v. Pub. Util. Comm.*, 63 Ohio St. 2d 62, 70 (1980).

Thus, it cannot be argued that Appellant could not foresee the exclusion of the costs of cancelled plants on the basis that they were not related to the provision of utility service as required by Ohio ratemaking law.

Likewise, Appellant should be aware that the Ohio court has disallowed a utility the recovery of costs which were non-recurring past losses in spite of the fact that the expenditures were required by Ohio Rev. Code §4905.22. In denying recovery of the costs of purchased power incurred at the direction of a temporary Commission order during a coal strike, the court said:

> Dispositive of appellant's claim of an unjust taking of property is the fact that appellee simply ordered appellant to do only that which appellant had a statutory obligation to provide for the public.
>
> * * * *
>
> R.C. 4905.22, which reads in the imperative, states that appellant *must* furnish adequate service to its customers . . .
>
> * * * *
>
> Therefore, appellee imposed no new or additional obligations upon appellant but rather reaffirmed existing statutory obligations. Therefore, there was no taking of private property and, thus, no due process violations.
>
> * * * *
>
> Finally, it is noted that a public utility has no constitutional right to recover past and unre-

covered costs through present and future rates. *Bluefield W.W. & Improvement Co. v. Public Service Comm.*, (1923) 262 U.S. 679.

C&SOE v. Pub. Util. Comm., 64 Ohio St. 2d 175, 177-178 (1980). *(Cert. den.*, ___ U.S. ___ (1981)).

Consequently, Appellant knew or should have known that there was nothing novel in the Ohio court's definition of allowable operating expenses as applied to the costs of cancelled generating plants. Furthermore, there is nothing in that definition or application which is inherently unconstitutional.

Beyond any shadow of doubt, the Ohio Supreme Court has in years past addressed the issue of what costs may be included to determine the annual operating expenses of a utility. For the Appellant to argue, that it was surprised at the Ohio Supreme Court's decision because the state court had not previously addressed the question of these specific costs, is an argument built on sand. The state court's earlier decisions were known, and could reasonably have been expected to be followed by that court.

Clearly, Appellant had the right *and* opportunity to present to the Ohio Supreme Court its constitutional arguments. It elected not to do so, and thus the Ohio Supreme Court was never given the opportunity to be presented with and thereafter expressly rule upon the constitutional issues. Based upon the sound logic expressed in the *Webb* decision, and those other decisions in which this Court refused to accept jurisdiction, Appellee Office of the Consumer's Counsel submits that its Motion to Dismiss is well taken and should be sustained.

MOTION TO AFFIRM

Appellant has presented this Court with two grounds pursuant to which it claims plenary consideration should be had. The first relates to Appellant's argument that the Ohio Supreme Court erred in its interpretation of an Ohio statute. The second argument asserts that the Ohio Supreme Court's decision in this case is in conflict with the decision of this Court in *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944). Both arguments are without merit, and this Court should affirm the ruling of the Ohio Supreme Court.

With respect to Appellant's first jurisdictional argument, the Ohio State Supreme Court in *Consumers' Counsel v. Public Utilities Commission* specifically limited its decision to "whether the cancelled plant expenditures represent '[t]he cost to the utility of rendering the public utility service for the test period.'" 67 Ohio St. 2d 153, 163, 423 N.E. 2d 820, 827 (1981). Regardless of the appellant's assertions to the contrary, it is clear that the Ohio court strictly limited its determination as to what costs appropriately fall within the meaning of Ohio Rev. Code §4909.15 (A) (4). Therefore, even if a federal question *had* been raised, it could only concern the state court's narrow holding in the case below and does not involve Ohio Rev. Code §4905.22.

Also, the fact that Appellant's decisions, to plan and subsequently cancel the plans to build the nuclear facilities, were prudent, is not relevant to this Court's decision. This investment "never provided any service whatsoever to the utility's customers." *Consumers' Counsel*, 67 Ohio St. 2d at 164,

423 N.E. 2d at 827. The Ohio court further found that "R.C. 4909.15 (A) (4) is designed to take into account the normal, recurring *expenses incurred by utilities in the course of rendering service to the public* for the test period." *Id.* (Emphasis added). Hence, it is clearly apparent that the decision below was derivative of the plain meaning of the statute's language. CEI investors have no statutory right to recover their investment, through amortization as service-related costs, when that "investment ***never provided any service whatsoever." *Id.* In reaching this holding, the Ohio Supreme Court was fairly interpreting the law of the State of Ohio. This Court should affirm the Ohio court's decision as the United States Supreme Court has stated that state "courts have the final authority to interpret, and where they see fit, to reinterpret [their] State's legislation." *Garner v. Louisiana*, 368 U.S. 157, 169 (1961).

Appellant further argues that its property, meaning the investment in the terminated nuclear plants, has been confiscated in violation of the fourteenth amendment to the United States Constitution. In support of this contention the appellant directs this Court's attention to *Bluefield Water Works Co. v. Public Service Commission*, 262 U.S. 679 (1923). *Bluefield* mandates that "a public utility is *entitled* to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public." 262 U.S. at 692-93. (Emphasis added). As this Court noted in *Bluefield:*

> Rates which are not sufficient to yield a reasonable return on the value of the property used, *at the time it is being used to render the service*, are unjust, unreasonable, and confiscatory, and their enforcement deprives the

> public utility company of its property in violation of the 14th Amendment.
>
> *Id.* at 290 (Emphasis added).

The investment in the cancelled plants was never used to render service to the public. Ohio Rev. Code §4909.15 (A) (4), as interpreted by the Ohio Supreme Court, establishes this same rule for the fixation of a public utility's rates. Ohio law, in accord with *Bluefield*, provides for the implementation of rates based upon property used to render service to the public. In this case, the Ohio court found that this investment was not even related to property which provided service to Appellant's customers. *Consumers' Counsel*, 67 Ohio St. 2d at 164, 423 N.E. 2d at 827. Thus, the appellant has not had property confiscated within the meaning of *Bluefield* and the fourteenth amendment.

The vital, yet unstated, premise in the Company's argument that its property has been unconstitutionally confiscated is that the "property" is the Company's investment in the cancelled projects. This view has its roots in Mr. Justice Brandeis' dissenting opinion in *Pacific Gas & Electric Co. v. San Francisco*, 265 U.S. 403 (1924). The federal courts have "recognized, however, that Justice Brandeis' formula for ascertaining rate base — the amount of capital prudently invested — was not to become the prevailing rule." *NEPCO Municipal Rate Committee v. FERC*, Case No. 80-1343, et al., slip op. at 8-9 (D.C. Cir., Oct. 15, 1981). Appellant's investment was related to property that never provided utility service to the public and whether or not this investment can be characterized as "property", which is doubtful, it is a cost that cannot lawfully be recovered from the Company's customers.

The Appellant purports to demonstrate to this Court that, "all other things being equal," the rates now set in response to the Ohio court's ruling are confiscatory. Jurisdictional Statement of Appellant, at 18-20. This reasoning is fraught with fault. Appellant has calculated its rate of return based upon numerous unstated variables and unsubstantiated assumptions. The Company simply states that the rate which would be achieved, absent the amortization of these costs, would fall below what the Commission determined to be just and reasonable. All other things cannot be equal as the Appellant so lightly assumes. Rates are not and cannot be determined in a vacuum. As this Court reasoned in *Bluefield*, the annual rate which "will *constitute just compensation depends upon many circumstances* and must be determined by the exercise of a fair and enlightened judgment, *having regard to all relevant facts*." 262 U.S. at 692-93. (Emphasis added). Since the rates have not convincingly been demonstrated to be unjust and unreasonable" . . . judicial inquiry under [the law] is at an end." *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944).

Notwithstanding the Appellant's allegations in its Jurisdictional Statement, this case does not present a federal question to the Court. The Ohio Supreme Court limited its decision to a construction of Ohio Rev. Code §4909.15 (A) (4), which defines allowable operating expenses as one facet of the ratemaking scheme set out in Ohio Law. This Court has articulated its awareness "that the [state] courts have the final authority to interpret and, where they see fit, to reinterpret [their] State's legislation." *Garner v. Louisiana*, 368 U.S. 157, 169 (1961). This recognition of the authority of state courts to construe state law, coupled with the

fact that there is no record evidence showing that the Ohio Court's interpretation of §4909.15 (A) (4) fixes confiscatory rates under Ohio's ratemaking formula, establishes that no federal question exists. Therefore, no reason remains for the United States Supreme Court to exercise its jurisdiction in this matter.

> It is a well-established principle of this Court that before [the Court] will review a decision of a state court it must *affirmatively appear* from the record that the federal question was presented to the highest court of the state having jurisdiction *and* that its decision of the federal question was *necessary* to its determination of the cause.
>
> *Durley v. Mayo*, 351 U.S. 277, 281 (1956) (Emphasis added).

As was previously discussed,the record herein is silent with regard to the confiscation issue. Since the Ohio Supreme Court's decision was strictly limited to a determination of state law, the resolution of a federal question, assuming for the purposes of argument one had been raised, was unnecessary to the determination of the cause.

Where both federal and state questions have been decided by the state court, "[it] is, of course, a familiar principle that this Court will decline to review state court judgments which rest on independent and adequate state grounds, even when those judgments also decide federal questions." *Henry v. Mississippi*, 379 U.S. 443, 446 (1965). The rationale for the adequate state ground rule was recently reiterated by this Court in *Zacchini v. Scripps-Howard Broadcasting Co.*: "our only power over state judgments is to correct them to the extent that they incorrectly adjudge federal rights." 433 U.S. 562, 566 (1977).

Therefore, due to the nonexistence of a federal question in this case this Court should affirm the decision of the Ohio Supreme Court. In addition, even if it is assumed, *arguendo*, that a federal question had been presented to the Ohio Supreme Court, that court rendered a decision only on a state question, thus leaving this Court with nothing over which to exercise its jurisdiction.

The second argument presented by Appellant is based upon this Court's decision in *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1944). The *sine qua non* of Appellant's argument on this point is stated in the first sentence of this section, wherein it asserts that the risk of excluding certain expenses has not been considered in setting the fair rate of return, "Thereby reducing the utility's effective overall net rate of return below the level expressly found to be fair, just and reasonable." Jurisdictional Statement of Appellant, p. 24.

In the first instance, there is no evidence that the Appellant is earning a rate of return below that which was found to be fair, just and reasonable. To consider only this one item of expense, as Appellant urges this Court to do, is to ignore the holding in *Bluefield W.W. & Improvement Co. v. Public Service Comm.*, 262 U.S. 683 (1923) that:

> What annual rate will constitute just compensation depends on many circumstances and must be determined by the exercise of a fair and enlightened judgement, having regard to *all* relevant facts.
>
> *Id.* at 692.

The result reached by the Ohio Supreme Court does not automatically result in a determination

that Appellant is earning a return below that which was found to fair, just and reasonable. As noted in *Bluefield*, "Investors take into account the result of past operations, especially in recent years, when determining the terms upon which they will invest is such an undertaking." *Id.* at 694. This taking into account by investors of recent operations must surely, therefore, take into account the belief of the Appellant as expressed to its investors that:

> CEI informed its investors in its "1979 Annual Report": "***The Company [CEI] will seek the approval of the Federal Energy Commission and the Public Utilities Commission of Ohio for authority to amortize [the costs previously expended toward the four nuclear units whose construction CAPCO terminated] over a suitable number of years. The extent to which these costs may be recovered through rates will be determined by the PUCO. If any costs of termination are not permitted to be recovered, the Company would be required to reduce net income by the disallowed amount. *In any event, the resolution of these matters should not have a material adverse impact on the financial position of the Company.*"
>
> *Consumers' Counsel v. Pub. Util. Comm.*, 67 Ohio St. 2d 153, 171, 423 N.E. 2d 820, (1981) (Emphasis added).

Appellant's investors, it must be presumed, took into account the statement by Appellant that disallowance of the construction expenses should have no material adverse impact on the financial position of the company, thus obviating the Appellant's argument the "CEI's investors did not anticipate the risk of exclusion from cost of service in Ohio and therefore did not cause the market to

reflect that risk in a higher required rate of return." Jurisdictional Statement of Appellant, p. 29.

Therefore, Appellee, the Office of the Consumers' Counsel submits that this Court should affirm the decision of the Ohio Supreme Court.

CONCLUSION

Appellant in this matter has failed to timely present for review by the Ohio Supreme Court the federal constitutional questions it would now have this Court review. The Ohio Supreme Court therefore never expressly passed upon the Appellant's constitutional challenge. This Court should therefore sustain Appellee's Motion to Dismiss this Appeal. In the alternative, Appellee submits that the decision of the Ohio Supreme Court should be affirmed based upon Appellee's Motion to Affirm.

Respectfully submitted,

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Case No. 81-1002

In the Supreme Court of the United States

October Term, 1981

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,

Appellant,

vs.

OFFICE OF CONSUMERS' COUNSEL, SENIOR CITIZENS COALITION, GREATER CLEVELAND WELFARE RIGHTS ORGANIZATION, INC., WESTERN RESERVE ALLIANCE, NORTH SHORE ALERT, CLEVELAND CHAPTER OF OHIOANS FOR UTILITY REFORM, CITY OF CLEVELAND,

and

THE PUBLIC UTILITIES COMMISSION OF OHIO,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF OHIO

REPLY BRIEF OF APPELLANT OPPOSING THE MOTIONS TO DISMISS OR AFFIRM

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TABLE OF CONTENTS

	Page
Table of Authorities	ii
Introductory Statement	1
Argument	2
I. APPELLANT ALERTED THE OHIO COURT TO THE POTENTIAL CONSTITUTIONAL PROBLEMS IN ITS FIRST BRIEF TO THAT COURT AND IMMEDIATELY QUESTIONED THE CONSTITUTIONALITY OF THE OHIO STATUTES, AS APPLIED, AT ITS FIRST OPPORTUNITY AFTER THE UNCONSTITUTIONAL CONSTRUCTION, IN ITS MOTION FOR REHEARING.	2
A. Appellee OCC has conceded that the Ohio Court decided the Federal questions raised	2
B. Appellant asserted "an explicit and timely insistence in the State Courts that a State statute, *as applied*, is repugnant to the Federal constitution . . ." *Charleston Federal Savings and Loan Assn. v. Alderson*, 324 U.S. 182, 185 (1944, emphasis added).	3
II. AS APPLIED BELOW, OHIO REVISED CODE § 4905.27 AND § 4909.15(A)(4) CONFISCATE APPELLANT'S PROPERTY WITHOUT DUE PROCESS OF LAW.	8
Conclusion	10
Exhibit 1 (Revised) – Chart of Terminated Units Pending Decision	1a
Exhibit 2 – OCC Memorandum Contra Company's Application For Rehearing, Case No. 81-1096-EL-COI	3a
Exhibit 3 – In The Matter Of The Investigation Of The Rates Of The Cleveland Electric Illuminating Company, Case No. 81-1096-EL-COI (Opinion and Order, October 21, 1981)	10a

TABLE OF AUTHORITIES

CASES

Bluefield Water Works v. Pub. Serv. Comm., 262 U.S. 679 (1923) 9

Brinkerhoff – Paris Trust and Savings Company v. Hill, 281 U.S. 673 (1930) 5

Charleston Federal Savings and Loan Assn. v. Alderson, 324 U.S. 182, 185 (1944, emphasis added) 3, 4

Columbus & Southern Ohio Electric Co. v. Pub. Util. Comm., 64 Ohio St. 2d 175, 413 N.E. 2d 1208, (1980), app. dismd. 69 L.Ed. 2d 948, 101 S. Ct. 3071 (1981) .. 6

Great Northern Railway Co. v. Sunburst Oil and Refining Co., 287 U.S. 358 (1932) 6

Missouri ex rel Missouri Insurance Co. v. Gehner, 281 U.S. 313, at 320 (1930) 5

Saunders v. Shaw, 244 U.S. 317 (1917) 5

STATUTES

Ohio Revised Code § 4905.18 4

Ohio Revised Code § 4905.22 ..... 4, 6

Ohio Revised Code § 4909.15(A)(2) 4

Ohio Revised Code § 4909.15(A)(3) 4

Ohio Revised Code § 4909.15(A)(4) 4

Ohio Revised Code § 4909.15(B) 4

INTRODUCTORY STATEMENT

Appellees Office of Consumers' Counsel (OCC), Senior Citizens Coalition, et al. (SCC), and City of Cleveland (City) have moved to dismiss this appeal. This Court should overrule those motions and allow plenary consideration.

Setting aside, for the moment, the conflicting positions of the Appellees and their misstatements of the record evidence and the law, we are impressed by the fact that none of them even so much as questions the hundreds of millions of dollars involved in pending cases on this precise issue all over the country. Indeed, the SCC expressly concedes (p. 34) that there are cases pending in other jurisdictions and suggests that this Court wait to hear one of those cases in fairness to the *other* utilities.

Since the writing of our Jurisdictional Statement, Boston Edison and Union Electric have cancelled planned generating units and the total amount involved in pending cases nationwide on this issue is now at least 1263.1 millions of dollars.[1]

Appellees do argue that this is a local matter affecting only Ohio. However, Appellee OCC has issued a press release to the opposite effect, which describes the Ohio Court's decision as "a landmark decision which establishes a national precedent." Further, the Ohio Court itself noted that "none of the previous rulings on this precise issue represents the opinion of the highest court of the jurisdiction in which the case arose." (67 Ohio St.2d at 162, reprinted at Appendix C-13). Indeed, the national financial press gave *this* case widespread publicity because of its uniqueness and importance to the utility industry.[2]

[1] Attached to this Brief as Exhibit 1 Revised is a chart showing the most recent information appellant could obtain regarding these pending cases.

[2] Copies of some of these articles are attached to CEI's Motion for Rehearing to the Ohio Court, which was reproduced for this Court as Exhibit 3 to CEI's Application For Stay, Case No. A-250.

Appellant respectfully submits that the monumental importance of this case to CEI and the utility industry requires resolution by this Court.

ARGUMENT

I. APPELLANT ALERTED THE OHIO COURT TO THE POTENTIAL CONSTITUTIONAL PROBLEMS IN ITS FIRST BRIEF TO THAT COURT AND IMMEDIATELY QUESTIONED THE CONSTITUTIONALITY OF THE OHIO STATUTES, AS APPLIED, AT ITS FIRST OPPORTUNITY AFTER THE UNCONSTITUTIONAL CONSTRUCTION, IN ITS MOTION FOR REHEARING.

A. Appellee OCC Has Conceded That The Ohio Court Decided The Federal Questions Raised.

Appellees move to dismiss arguing that the constitutional issues were not timely raised before, and not decided by, the Ohio Supreme Court. However, OCC has explicitly argued before the Commission in *this* case that the "constitutional arguments" made by Appellant CEI were the "identical issue(s)" which were "previously *passed upon* by the Ohio Supreme Court . . ." (emphasis added).

After the Ohio Supreme Court denied Appellant's Motion For Rehearing and issued its mandate to the Public Utilities Commission, the Commission initiated an investigation (Case No. 81-1096-EL-COI) regarding implementation of the Ohio Court's decision. This Court denied CEI's Application For Stay (Case No. A-250) and the procedure before the Commission went forward. In that proceeding, Appellant CEI argued that denial of any recovery of its prudent expenses in planning the cancelled units was an unconstitutional confiscation of its property, just as CEI had argued in the Ohio Court and in this Court. The Commission, being bound by the Ohio Court's decision, rejected CEI's arguments and reduced CEI's rates by

$6.7 million on an annual basis. Appellant CEI requested Rehearing before the Commission, a prerequisite to appeal.

Appellee OCC filed with the Commission, on November 30, 1981, a "Memorandum Contra Company's Application For Rehearing" in which OCC argued that CEI's constitutional arguments had been *decided* already by the Ohio Court and could not be asserted again under the doctrine or *rea judicata*:

> "In this proceeding the Company has attempted to raise several *constitutional arguments*, which, it believes, justify the inclusion of the expenses disallowed in *Consumers' Counsel v. Public Utilities Commission*, 67 Ohio St.2d 153 (1981). In *Consumers' Counsel, supra*, CEI was an Intervening Appellee, and availed itself of the opportunity to raise defenses in support of this Commission's initial decision in *Re Cleveland Electric Illuminating Company*, Case No. 79-537-EL-AIR, *Opinion and Order* (July 10, 1980). This attempt by CEI to reargue and relitigate the identical issue previously *passed upon* by the Ohio Supreme Court is barred by the doctrine of res judicata." (Emphasis added).[3]

In other words, Appellee OCC has recently argued in a brief to the Ohio Commission on this precise issue that the Ohio Court, in *this* case, "*passed upon*" the "identical issue" raised by Appellant in this Court. Appellee OCC cannot have it both ways. Under these circumstances, this Court should reject the arguments of Appellees that the constitutional questions were not timely raised or decided by the Ohio Court.

B. Appellant Asserted "An Explicit And Timely Insistence In The State Courts That A State Statute, *As Applied*, Is Repugnant To The Federal Constitution . . ." *Charleston Federal Savings and Loan Assn. v. Alderson*, 324 U.S. 182, 185 (1944, emphasis added).

[3] We have reprinted in full the OCC Memorandum as Exhibit 2 to this Brief.

Appellee City argues (p. 12) that the jurisdiction of this Court depends on "an explicit and timely insistence in the state courts that a state statute, *as applied*, is repugnant to the federal Constitution . . .," quoting *Charleston Federal Savings and Loan Assn. v. Alderson*, 324 U.S. 182, 185 (1944, emphasis added). That is precisely what Appellant did. Until the decision by the Ohio Court in *this* case, Ohio Revised Code Sections 4905.22 and 4909.15(A)(4), were not unconstitutional, *as applied*.

In the past, the Commission had required Appellant to account for these planning costs in a plant account (Account 107) and had excluded them from cost of service, under its Uniform System of Accounts, because these costs would become part of rate base when the plants were built and went into service. As part of rate base, an opportunity for a recovery *of* these costs would be accomplished through depreciation expense, as guaranteed by Ohio Revised Code Section 4905.18. An opportunity for a recovery *on* these costs would be accomplished by applying the allowed rate of return to the rate base, as guaranteed by Ohio Revised Code Sections 4909.15(A)(2), (A)(3) and (B).

If these planning costs had been *general* system planning costs (not associated with particular units), these costs would have been charged to an expense account (Account 500, Production — Operation, Supervision and Engineering), and would have been allowed as routine costs of service and charged to the rate-payers. Until the decision in *this* case, neither the Ohio Commission nor the Ohio Court had ever denied recovery of prudent planning and engineering costs dedicated to utility service in these circumstances, either as a capitalized cost allowed in rate base or as an allowable expense in cost of service.

When the planning for these units was stopped, recovery of these planning costs could not be accomplished through either of these regular methods. The Uniform

System of Accounts provided for this eventuality by the transfer of these costs from the property account (107) to an expense account (182), to be included in cost of service. Thus, Justice Paul Brown, in his Concurring and Dissenting Opinion in this case (See Appendix C-21), concluded that the Ohio Court's rejection of this procedure in the Uniform System of Accounts for the first time in this case was improper:

> "This accounting system has been in effect in Ohio for approximately two decades. Given this fact, we can reasonably assume that the General Assembly was cognizant of its existence when it amended R.C. 4909.15 in 1976, and that it was not the intent of the General Assembly to treat these extraordinary property losses in a different manner in which they were treated by the Public Utilities Commission." (67 Ohio St. 2d at 170, reprinted at Appendix C-22).

No case or Commission decision in Ohio, until *this* case, had ever excluded reasonable and prudent general planning and engineering expenses from cost of service. The Ohio Court cited no precedent in its decision below, and the cases cited by Appellees are completely inapposite.

When the Ohio statutes were rendered unconstitutional, "as applied" in *this* case, CEI "at the first opportunity,[4] invoked the protection of the Federal Constitution. . . . It could not earlier have assailed the [statutes] as violative of the Constitution . . ." because the statutes had never previously been so applied. *Missouri ex rel Missouri Insurance Co. v. Gehner*, 281 U.S. 313, at 320 (1930). *See also Saunders v. Shaw*, 244 U.S. 317 (1917); *Brinkerhoff – Paris Trust and Savings Company v. Hill*, 281 U.S. 673 (1930);

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[4] A copy of CEI's Motion For Rehearing may be found as Exhibit 3 to CEI's Application For Stay to this Court, which was assigned Case No. A-250. No Appellee has argued that the Motion For Rehearing failed to elaborate on CEI's constitutional objections.

Great Northern Railway Co. v. Sunburst Oil and Refining Co., 287 U.S. 358 (1932).[5]

Despite its agreement that an appellant to this Court is "*not* bound to anticipate the *eventual construction* placed on a statute by the state supreme court" (OCC Brief, p. 12), OCC nevertheless asserts that jurisdiction in this Court should be denied because CEI did not "elaborate" on its constitutional argument at page 21 of its initial brief to the Ohio Court. OCC argues that CEI was required to "elaborate" because the *result* denying the cost was foreseeable, since the Ohio Court had previously sustained the Commission in refusing recognition in rates of other kinds of costs, citing *Columbus & Southern Ohio Electric Co. v. Pub. Util. Comm.*, 64 Ohio St. 2d 175 (1980), *app. dismd.* 69 L.Ed.2d 948 (1981). That case, like the other cases cited by Appellees to support their foreseeability argument, is simply inapplicable to the facts here.

In *Columbus & Southern*, the Commission held that a coal strike which lasted several weeks was a non-recurring event and that therefore the costs of purchased power during the strike were non-recurring costs which should not be relied upon in setting reasonable rates for the future. Since the utility had a mandatory statutory duty under Ohio Revised Code § 4905.22 to "furnish adequate service to its customers . . ." which required it to purchase power from another utility when necessary, the order of the Commission directing the utility to do so "imposed no new or additional obligations" and no new risk which was not already compensated in rate of return.

In contrast, in the present case the uncontroverted evidence (despite the claim by the City) is that the investor anticipated only the risk of exclusion of imprudent

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[5]For a more thorough discussion of this line of cases, please refer to CEI's Supplemental Brief In Support Of Application For Stay in Case No. A-250, which was filed with this Court on September 29, 1981.

expenditures, *not* the risk that concededly *prudent* expenditures would be excluded. In *Columbus & Southern*, the eminently predictable Commission order did not create any additional risk not already compensated through rate of return, so there was no confiscation. In the present case, the entirely unforeseeable construction of the Ohio statutes by the Ohio Court denied CEI the opportunity for recovery *of* its prudent expenses and the uncontroverted evidence showed that the investor had *not* been compensated through rate of return on by any other mechanism.

In the present case, the Ohio Court does not hold that *general* system planning and engineering costs must be excluded from rates.[6] The *only* reason that the present planning and engineering costs were excluded from CEI's rates is that they constituted an "investment in unfinished projects ineligible for rate base treatment. . . ." (67 Ohio St.2d at 166, reprinted at Appendix C-18). In other words, the Ohio Court excluded these concededly prudent planning costs from rates only because the Uniform System of Accounts required that they be capitalized to a property account for one particular "unfinished project(s)" which later became "ineligible for rate base treatment." Had CEI violated the Uniform System of Accounts and expensed these planning and engineering costs to the expense account used for *general* system planning costs (Account 500), there would have been no question as to their includability in cost of service.

Appellant CEI was surprised by the Ohio Court's decision applying the statutes this way for the first time, and the reasons for the surprise are obvious. As the Ohio Court itself noted, "the overwhelming weight of authority

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[6]Indeed, in another section of its Opinion, dealing with the excess capacity issue, the Ohio Court explicitly acknowledges the "difficulties" the utilities face and the need for utilities to "anticipate load growth years in advance to maintain adequate capacity to ensure reliable service." 67 Ohio St.2d at 158.

from other jurisdictions" supported the Commission's allowance of the expense. Indeed, the Ohio Court itself cited eleven (11) such decisions supporting the Commission's decision, and we have cited thirty-one (31) such decisions to this Court, without dispute from any Appellee.

Appellees argue that the cautionary language in CEI's Annual Report To Shareholders shows that the Ohio Court's "eventual construction placed on [the] statute" was foreseeable. Nothing could be further from the truth. CEI had an obligation to alert its stockholders and the financial community that the matter was subject to litigation. While it was conceivable that the planning expenses might have been excluded as imprudent, it was entirely unforeseeable that the expenses would be found to have been "reasonable and prudent at every step of the process" and found to have been "costs incurred on behalf of its ratepayers to assure that adequate service could be maintained" and *nevertheless* be disallowed by the Ohio Court.

II. AS APPLIED BELOW, OHIO REVISED CODE § 4905.27 AND § 4909.15(A)(4) CONFISCATE APPELLANT'S PROPERTY WITHOUT DUE PROCESS OF LAW.

On October 21, 1981, the Public Utilities Commission of Ohio ordered CEI's rates reduced by the amount of the planning expenses, effective October 28, 1981.[7] That order made no provision for the confiscation which resulted and no provision for the additional risk and consequently higher cost of capital suffered by CEI as a result of the Ohio Court's decision.

Contrary to the City's unsupported assertions, the unanimous testimony of every witness who addressed the

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[7]This Opinion and Order of the PUCO (Case No. 81-1096-EL-COI) reducing CEI's rates is reprinted as Exhibit 3 to this Brief.

subject was that the investor did *not* anticipate such a decision against "the overwhelming weight of authority" and was *not* compensated for the risk that prudent expenses dedicated to the ratepayer would be disallowed. CEI witnesses Maugans and Jeffries and Commission Staff witnesses Hanna and Farrar *unanimously* so testified. No witness testified to the contrary.

It is plain that a rate of return which is reasonable when the planning costs are allowed is simply not a reasonable rate of return if the planning costs are removed from the allowed rates. There is no great complexity to calculating the impact of the required one-time write-off of $56.4 Million to determine the confiscatory overall rate of return (6.4%) which results.

Appellee OCC argues that CEI's calculation is improper because "All other things cannot be equal as the Appellant so lightly assumes. Rates are not and cannot be determined in a vacuum." Yet in the Commission's recent investigation which lowered CEI's rates because of the Ohio Court's decision in this matter, the OCC argued precisely the opposite position.[8] The Commission addressed only the single issue and reduced CEI's rates in precisely the "simplistic fashion" sought by OCC. Again, this Court should note that OCC's positions here and before the Commission are amazingly contradictory. This Court must not allow OCC to do an 'about-face' now and attack the calculation of the resulting confiscatory rate of return (6.4%). *Bluefield Water Works v. Pub. Serv. Comm.*, 262 U.S. 679 (1923) *and its progeny.*

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[8]As the Commission noted in its Opinion, "OCC and the City of Cleveland contend that the order of the Supreme Court was specifically directed to a *single issue* and that changes that may have taken place in other items since the establishment of these rates *need not be considered.*" (Case No. 81-1096-EL-COI, Opinion and Order, p. 3, reprinted as Exhibit 3 to this Brief.)

CONCLUSION

The Ohio Court explicitly said that "We must decide whether the test of prudence . . . is consistent with the . . . ratemaking formula. . . ." The Ohio Court assumed the prudence of the investments, as found by the Commission, and held that *nevertheless* they could not be recovered by the utility. This case therefore presents this Court with a clear-cut issue: Is it lawful for a state to require prudent investment by a public utility to insure rendition of utility service and to simultaneously prohibit the utility from any opportunity whatsoever for recovery *of* that prudent investment, much less for earning a return *on* it? A state statute which requires such a result, as applied, plainly confiscates the utility's property. The issue has never before come up in Ohio and would not exist now but for the unique interpretation placed upon the Ohio statutes by the Ohio Supreme Court.

For the foregoing reasons, the questions presented are so substantial as to require plenary consideration, with briefs on the merits and oral argument, for their resolution, and the Motions To Dismiss should be denied.

Respectfully submitted,

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EXHIBIT 1
(Revised)

Company/Unit	State or Jurisdiction	Cost (Million)	Type	Litigation
Rochester Gas & Electric/Sterling	New York State Public Service Commission	$29.5	Nuclear	Hearings pending with NYSPSC with current Rate Case pending outcome.
Niagara Mohawk Power Corp./ Sterling	New York State Public Service Commission	$17.3	Nuclear	Case pending with NYSPSC.
Central Hudson/ Sterling	New York State Public Service Commission	$15	Nuclear	Case pending with NYSPSC.
Orange & Rockland Utilities Inc./ Sterling	New York State Public Service Commission	$29.4	Nuclear	Case pending with NYSPSC but rate case not postponed.
Long Island Light Co./James Port 1 & 2	New York State Public Service Commission	$39	Nuclear	Not yet claimed but proceedings to follow.
Jersey Central Power & Light/ Forked River	New Jersey Public Utility Commission	$4.2	Nuclear	Current proceeding with Public Utility Commission.
Mississippi Power and Light/Dasota County	Mississippi Public Utility Commission	$1.7	Coal	Will appeal to State Supreme Court on Commissions 70% allow. amortization decision.
New England Power Company/Salem Harbor 5	FERC	$12.5	Fossil-Oil	Issue of rate base and amortization before D.C. Court of Appeals (will appeal to Supreme if necessary).
New England Power Company and Partners/Montague 1 & 2	FERC	$70	Nuclear	Not yet claimed but proceedings to follow.
Detroit Edison/ Greenwood 2 & 3	Michigan Public Utility Commission	$70	Nuclear	Case pending.

EXHIBIT 1 (continued)

Company/Unit	State or Jurisdiction	Cost (Million)	Type	Litigation
Wisconsin Power & Light/Koshkohong	Wisconsin Circuit Court	$7.0	Nuclear	Commission ruled in favor of amortization with Circuit Court now reviewing.
Central Maine Power/Richmond & Sears Island	Maine Public Utilities Commission	$3.5	Coal	In Appeals Court to review Maine Comm. Decision.
Northern States Power/Tyrone Energy Park 1	Wisconsin Pub. Util. Com., North Dakota District Court, Minnesota District Court & FERC	$67	Nuclear	Appeals in District Court in N. Dakota and Minn.
Portland General Electric/Pebble Springs 1 & 2	Oregon Public Utilities Commission	$61	Nuclear	Plant cancelled at Oregon site, pending relocation; likely to sue for current costs.
Pudget Sound Power & Light/ Pebble Springs 1 & 2	Oregon Public Utilities Commission	$30	Nuclear	Plant cancelled at Oregon site, pending relocation; likely to sue for current costs.
Pacific Power and Light/Pebble Springs 1 & 2	Oregon Public Utilities Commission	$38	Nuclear	Plant cancelled at Oregon site, pending relocation; likely to sue for current costs.
Northern Indiana Public Service/ Bailey 1	Indiana Public Utilities Commission	$205	Nuclear	Plans cancelled, proceedings to follow.
Boston Edison and partners/Pilgrim 2	Massachusetts	$493	Nuclear	Plant cancelled, rate case filed and pending
Union Electric/ Callaway Unit 2	Missouri	$70	Nuclear	Plant cancelled, proceedings to follow
Total: 26 Units	11 Jurisdictions	$1,263.1 millions		

EXHIBIT 2

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Investigation of the Rates of the Cleveland Electric Illuminating Company.	))))	**Case No. 81-1096-EL-COI**

MEMORANDUM CONTRA COMPANY'S APPLICATION FOR REHEARING

First of all, it must be noted that the Company's arguments in support of its Application for Rehearing bring nothing new to the long debated issue, but rather reiterate arguments previously presented by Cleveland Electric Illuminating Company (CEI). OCC, however, will briefly address several of the "alleged" errors raised by the Company.

Initially, the Company is heard to challenge the legality of the proceeding. The Commission initiated this proceeding pursuant to Ohio Revised Code, Section 4905.26 which allows the Commission to investigate and determine whether the rates of a utility are fair, just and reasonable. The Company, on oral agreement, acknowledged that this was the appropriate mechanism in which to address the complex issue:

> (By Mr. Buchmann): Now, two other things are a point. *We come up then into this investigation which it seems to me is the proper vehicle to resolve the difficulty caused by one rate case being superseded by another.*
>
> (Tr. of October 13, 1981 at 18). (Emphasis added)

Yet, now the Company is heard to object to this investigation as being an inappropriate mechanism for determining whether CEI's rates should be reduced. Having acknowledged that this is the appropriate proceeding in which to deal with the issue, the Company cannot now complain that the proceeding was improper.

In this proceeding the Company has attempted to raise several constitutional arguments, which, it believes, justify the inclusion of the expenses disallowed in *Consumers' Counsel v. Public Utilities Commission*, 67 Ohio St.2d 153 (1981). In *Consumers' Counsel, supra,* CEI was an Intervening Appellee, and availed itself of the opportunity to raise defenses in support of this Commission's initial decision in *Re Cleveland Electric Illuminating Company,* Case No. 79-537-EL-AIR, *Opinion and Order* (July 10, 1980). This attempt by CEI to reargue and relitigate the identical issue previously passed upon by the Ohio Supreme Court is barred by the doctrine of res judicata.

In *State ex rel Hamilton v. Public Utilities Commission,* 10 Ohio St.2d 172 (1967) the City of Hamilton sought a Writ of Prohibition to prevent the Public Utilities Commission from considering an application filed by the Cincinnati Gas & Electric Company (CG&E). The application, filed on November 26, 1966, sought disapproval of the City's termination of a gas purchase agreement with CG&E. The application was made, purportedly, under the Miller Act. Previously CG&E had sought injunctive relief, seeking to enjoin termination of the contract until such time as the Public Utilities Commission had approved the proposed termination. The Court of Common Pleas denied the injunctive relief. The decision was appealed to the Court of Appeals, which affirmed the decision of the Court of Common Pleas. An appeal from the decision by the Court of Common Pleas, as affirmed by the Court of Appeals, was denied by the

Supreme Court. In granting the City's requested Writ of Prohibition, to prevent a relitigation of the proposed elimination before the Commission, the Ohio Supreme Court stated:

> Per Curiam. The questions raised by respondent in this action were determined in the foregoing injunction case in Butler County. *Relator was a party to that action and respondent, although* not a party, upon appeal *appeared as amicus curiae in the Supreme Court.* Furthermore, *the real party interested in sustaining respondent's position in this case is Cincinnati Gas & Electric Company, which was a party in the Butler County case. Under such circumstances, the issue is res judicata.*
>
> *State ex rel Hamilton, supra* at 174. (Emphasis Added).

In *Grubb v. Public Utilities Commission*, 281 U.S. 470 (1930) the U.S. Supreme Court was faced with a similar issue. The Appellant, in *Grubb* sought from the Public Utilities Commission of Ohio a certificate to operate a passenger line through the state. The certificate was granted in part and denied in part. A rehearing was sought by Appellant which was denied. Following the denial of the rehearing Appellant brought suit in the Federal district court seeking injunctive relief. While the suit in district court was pending, the Supreme Court of Ohio heard an appeal by the Appellant, and issued an opinion. Following the decision adverse to the Appellant, the district court proceeding was dismissed on the grounds that Appellant was barred and estopped from further litigation of the issue. The Appellant sought a reversal by the U.S. Supreme Court of the Federal court dismissal. In reviewing Appellant's arguments the Court noted that Appellant was now attempting to raise an issue not

specifically brought to the attention of the state court. In discussing that argument the Court stated:

> *In his bill the appellant assails the validity of the order upon one ground not brought to the attention of the state court* – a ground arising out of the granting to another interstate motor line of a certificate to operate busses over a route including the loop at Portsmouth; *and he insists that this ground of objection is not concluded by the judgment of the state court, and therefore is open to examination and adjudication upon its merits by the district court.* But the judgment has a broader operation as res judicata than is thus suggested. The certificate referred to was granted several months before the appellant applied for a certificate and he had personal knowledge of it from the time it was granted. It was shown upon the records of the commission and was easily accessible when the hearing was had upon his application. Thus it is a matter which, if having the bearing now suggested, could have been brought to the attention of the commission either at that hearing or in his request for a rehearing (543, General Statutes); and, if it was not then given proper effect, he could have brought it to the attention of the state court and have made the same claim in respect of it that is now made in his bill.
>
> *The thing presented for adjudication in the case in the state court was the validity of the order, and it was incumbent of the appellant to present in support of his asserted right of attack every available ground of which he had knowledge.*
>
> He was not at liberty to prosecute that right by piecemeal, as by presenting a part only of the available grounds and reserving others for another suit, if failing in that.
>
> *Grubb, supra* at 478. (Emphasis Added).

The Court went on to further indicate:

> *As the ground just described was available but not put forward, the appellant must abide the rule that a judgment upon the merits in one suit is res judicata in another where the parties and subject-matter are the same,* not only as respects matters actually presented to sustain or defeat the right asserted, but also as respects any other available matter which might have been presented to that end.
>
> *Grubb, supra* at 479. (Emphasis Added.)

In this instance CEI was a *party* to the prior proceeding. The Company had ample opportunity to present all arguments in support of the Commission's decision in *Re Cleveland Electric Illuminating Company, supra.* Having had one opportunity to litigate the issue the Company is now barred from doing so a second time.

OCC has not replied to each item raised by the Company, even though the OCC is in strong disagreement with CEI's list of "alleged" errors. The OCC believes that each of the points not specifically addressed in this reply has been thoroughly argued in OCC's previously filed pleadings, and OCC's final argument. OCC does not wish to burden the Commission with repetitive arguments, but will simply rely upon these previous discussions.

CEI having acknowledged that the procedure adopted by the Commission was the proper procedure, cannot now be heard to object. CEI's attempts to relitigate the includability of the expenses also must fail. This attempt to relitigate the issue is barred by the doctrine of res judicata.

WHEREFORE, OCC respectfully requests the Commission deny CEI's Application for Rehearing in the above captioned proceeding.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that copies of the Memorandum have been served by first class mail, postage prepaid, or hand-delivered, to the following parties of record on this 30th day of November, 1980:

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EXHIBIT 3

BEFORE

THE PUBLIC UTILITIES COMMISSION

OF OHIO

In the Matter of the Investigation of the Rates of The Cleveland Electric Illuminating Company.	Case No. 81-1096-EL-COI

OPINION AND ORDER

The Commission, coming now to consider the above-entitled matter, having reviewed the arguments introduced at public hearing and the briefs of the parties, and being fully advised of the facts and issues in this case, hereby issues its Opinion and Order.

APPEARANCES:

Mr. Alan D. Wright, General Counsel, and Mr. Craig I. Smith, Senior Counsel, 55 Public Square, Cleveland, Ohio, and Messrs. Squire, Sanders & Dempsey, by Mr. Alan P. Buchmann, 1800 Union Commerce Building, Cleveland, Ohio, on behalf of the Applicant, The Cleveland Electric Illuminating Company.

Mr. William J. Brown, Attorney General of Ohio, by Mr. Marvin I. Resnik, Mrs. Marsha Rockey Schermer and Mr. Jonathan L. Heller, Assistant Attorneys General, 375 South High Street, Columbus, Ohio, on behalf of the Staff of the Public Utilities Commission of Ohio.

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Messrs. Bell & Cievenger, L.P.A., by Messrs. Langdon D. Bell and Samuel C. Randazzo, 21 East State Street, Columbus, Ohio, on behalf of the Industrial Electricity Consumers.

HISTORY OF THE PROCEEDINGS:

In its Opinion and Order of July 10, 1980 in Case No. 79-537-EL-AIR, and in the May 4, 1981 Opinion and Order in Case No. 80-376-EL-AIR, the last two rate proceedings involving The Cleveland Electric Illuminating Company (CEI), the Commission authorized the inclusion in allowable expenses of the amortization of CEI's share of the costs associated with the cancellation of four nuclear plants. On appeal of the decision in Case No. 79-537-EL-AIR, the Ohio Supreme Court found that the inclusion of those costs was unreasonable and unlawful. *Consumers' Counsel v. Public Utilities Commission*, 67 Ohio St. 2d 153 (1981). In light of that decision, the Commission initiated this investigation of CEI's rates, pursuant to Section 4905.26, Revised Code, by Entry dated September 16, 1981.

The decision of the Supreme Court of Ohio in *Consumers' Counsel v. Public Utilities Commission, supra*, was reported on July 19, 1981. Issuance of the Court's mandate, however, was stayed, pursuant to Supreme Court Rule IX, Section 2, by the filing of an application for rehearing by CEI: The application for rehearing was denied by Supreme Court Entry dated September 1, 1981, and the Court issued its mandate. Promptly, CEI filed a motion for a stay of the

mandate which was denied by the Supreme Court of Ohio on September 11, 1981. On September 2, 1981, CEI filed with the Supreme Court of Ohio a notice of appeal to the United States Supreme Court and on September 22, 1981, CEI applied to the United States Supreme Court for a stay of the execution of the mandate of the Ohio Supreme Court. The application for a stay to the United States Supreme Court was denied on October 13, 1981.

Pursuant to the Commission Entry of September 16, 1981 a prehearing conference was held in this matter on September 23, 1981. At that time it was decided that briefs would be submitted by the parties and that the hearing scheduled for October 13, 1981 would be limited to oral argument on the briefs. The hearing was conducted on October 13, 1981 and the record certified to this Commission for appropriate action.

The parties hereto are The Cleveland Electric Illuminating Company (CEI or Company), the Office of the Consumers' Counsel (OCC), the City of Cleveland (City) and the Industrial Electric Consumers (IEC), the latter three having been granted leave to intervene by entry or ruling at the hearing held on October 13, 1981. A petition to intervene filed by Senior Citizens, et al. was denied by the attorney examiner by entry of October 8, 1981, and no appeal to the Commission has been taken.

COMMISSION REVIEW AND DISCUSSION:

The issue before the Commission at this time is the selection of an appropriate method for implementing the mandate issued by the Supreme Court of Ohio on September 1, 1981. This issue is clouded, however, by complexities that are beyond the control of this Commission or any of the parties appearing before it. The mandate issued by the Supreme Court of Ohio was issued in Commission Case No. 79-537-EL-AIR, Opinion and Order issued July 10,

1979. The rates for electric service authorized and established in Case No. 79-537-EL-AIR were found to be unreasonable and, therefore were, supplanted by those rates established by the Commission in Case No. 80-376-EL-AIR, Opinion and Order issued May 4, 1981. In Case No. 80-376-EL-AIR the Commission also allowed the annual amortization of the costs associated with the cancelled nuclear plants as part of operating expenses for rate making purposes. No appeals from that aspect of the Commission's decision are pending.[1] In addition, the Company has another rate case pending in Case No. 81-146-EL-AIR, based upon a more current test year, which should commence hearings in late 1981 or early 1982. Thus, although the mandate issued by the Court is clear in its intent, the intent of the Court as to how it is to be implemented may not be.

As noted, this Commission could implement the Court's decision in one of several ways. First of all it could conduct an investigation of the rates established in Case No. 79-537-EL-AIR, although clearly this would be a meaningless exercise. The Commission could simply reduce the rates currently in effect by virtue of Case No. 80-376-EL-AIR by an amount equal to the amortization adjustment; this would ignore, however, all other changes in circumstance that have occurred since the implementation of those rates. Or the Commission could apply the mandate of the Supreme Court on a prospective basis in Case No. 81-146-EL-AIR, which will commence hearings in a few months. The Commission, however, has chosen to implement the Supreme Court's mandate through the initiation of this proceeding. We believe that this is the best

[1] It should be noted that intervenor Senior Citizens, et al., noticed an appeal, which appeal is presently pending, which did raise the issue of the lawfulness of the inclusion of the amortization in allowable expenses. By letter dated September 3, 1981, Senior Citizens, et al., notified the Court that it would not pursue that issue.

method to effectuate the Supreme Court's mandate in the most expedient fashion.

The Office of Consumers' Counsel (OCC) and the City of Cleveland both contend that the remand of the Supreme Court of Ohio requires that this Commission immediately redetermine CEI's allowable operating expenses excluding therefrom the expenditures attributable to the cancelled nuclear facilities and reduce CEI's current rates accordingly. OCC and the City of Cleveland contend that the order of the Supreme Court was specifically directed to a single issue and that changes that may have taken place in other items since the establishment of these rates need not be considered. The City of Cleveland and OCC contend that the adjustment can be made on the data available to the Commission in the most recent rate proceeding. In essence, these parties contend that this Commission should apply the remand of Case No. 79-537-EL-AIR to Case No. 80-376-EL-AIR in a simplistic fashion. The problem, of course, is that CEI's present rates were fixed not in Case No. 79-537-EL-AIR, but in Case No. 80-376-EL-AIR, and there is no remand or mandate in the latter.

The Company contends that the rates established in Case No. 80-376-EL-AIR are presumptively just and reasonable pursuant to Section 4909.15, Revised Code, and the Supreme Court's decision in the prior rate case does not change this presumption. The Company contends that the decision of the Supreme Court should not result in an automatic adjustment of previously-established rates.

In the alternative, the Company contends that if the Supreme Court decision is deemed a sufficient basis for the institution of an investigation into the current rates, such an investigation must consider more than a single item subtracted from the Company's allowable expenses. The Company points out that the test period in Case No. 80-376-EL-AIR was the calendar year 1980, and that we

are currently through most of 1981 and a great number of the circumstances have changed. The Company contends that in order to make a determination that CEI's rates should be reduced, this Commission must consider more than the one expense item dealt with by the Supreme Court. The Company points out that the theories behind rate making and the test year concept do not provide for an item by item guaranteed dollar-for-dollar recovery, but rather the establishment of a reasonable allowance for a normal and necessary utility function. The Company argues that although the Supreme Court has stated that the abandonment loss can no longer be considered in establishing this "reasonable allowance", it does not necessarily follow that it must be removed from a reasonable allowance established in the past, without considering all of the elements that make up that allowance.

A further complicating factor is that we are not concerned solely with the inclusion in rates of this expense, but with the impact of the disallowance of the same, requiring careful consideration of all of the implications of such disallowance on the accumulated deferred balances being amortized. Some of those implications were discussed in the Commission's Opinion in Case No. 79-537-EL-AIR and their significance was indicated in Ohio Edison, Case No. 81-898-EL-AEM. The potential influence on the cost of capital and the financial standing of CEI should not be overlooked.

The Commission, thus, is confronted with a series of involved and inter-related problems. In the first instance, it cannot meaningfully act directly on the remand, because the remand is in a case which has since been superseded. Similarly, we must reject OCC's request (OCC Brief p. 5) that we calculate CEI's allowable expenses "based upon the test year data in the remand proceeding," which is the 1979 data while CEI's present rates are based on a 1980 test year. On the other hand, CEI's argument that we must,

in effect, conduct a new rate case now seems impracticable in view of the fact that hearings should be conducted in the relatively near future in Case No. 81-146-EL-AIR in which the adequacy of CEI's present rates may be fully explored. The Commission does not mean to say that it is appropriate or, even for that matter, lawful, generally speaking, to adjust rates by a single item because of events occurring after its decision nor, conversely, that the technical status of a case or series of cases should be employed to promote form over substance. We believe that a practicable solution is required and that the basic thrust of the Ohio Supreme Court's decision in *Consumers' Counsel v. Public Utilities Commission, supra,* can be implemented in these circumstances, while preserving the legal rights of the utility. In a sense, the fact that the rates set in Case No. 79-537-EL-AIR have been superseded in Case No. 80-376-EL-AIR is, as a practical matter, counterbalanced by the fact that rates set in Case No. 80-376-EL-AIR will, presumably, soon be superseded in Case No. 81-146-EL-AIR.

The Commission concludes, therefore, that CEI should be directed to file tariffs which reduce its present rates. The Commission is mindful, however, that CEI's appeal to the United States Supreme Court is still pending and that CEI has stated that it intends to pursue that appeal vigorously. In order to obviate any future questions with respect to the amount foregoing through this rate reduction, therefore, CEI is authorized and directed to maintain the same in the appropriate deferred reserves. Such reserves, including this presently foregone amortization, should be maintained by CEI pending a final decision on the lawfulness of the inclusion of these costs in allowable expenses for rate-making purposes or such action as the Commission may take after a full review of all aspects of this question in CEI's pending electric rate case. Obviously, if CEI should eventually prevail on its appeal to the United States Supreme Court, this will do no more than temporari-

ly postpone the recovery of these costs while, in the meantime, CEI consumers will receive the present rate relief which we believe the Ohio Supreme Court expected and which the intervening parties have requested. The Commission will also be able in the context of a full rate case, to consider all of the implications of the Ohio Supreme Court's decision and take such pertinent action as it may deem appropriate.

ORDER:

It is, therefore,

ORDERED, That The Cleveland Electric Illuminating Company submit tariffs for the approval of this Commission, reducing its present rates by an amount equal to the revenue requirements attributable to the cancelled nuclear facilities included therein. It is, further,

ORDERED, That The Cleveland Electric Illuminating Company submit three (3) complete copies of the tariffs by October 26, 1981, to be reviewed by the Commission and approved by subsequent entry. It is, further,

ORDERED, That The Cleveland Electric Illuminating Company continue to defer the accumulated amounts, including the amounts which would have been amortized but for this rate reduction, on its books, as part of the presently accrued deferred reserves with respect to such costs, pending further direction from this Commission and that, at the time it submits the tariffs required by the preceding paragraph of this order, it submit to the Commission's accounting staff the details of the accounting procedures by which it intends to maintain such deferral. It is, further,

ORDERED, That a copy of this Opinion and Order be served on all parties of record in this proceeding.

THE PUBLIC UTILITIES COMMISSION OF OHIO

JON F. KELLY
(Chairman)

DENNIS PINES

MICHAEL DEL BANE
(Commissioners)

Entered in the Journal
OCTOBER 21, 1981

A True Copy
DAVID M. POLK
David M. Polk
Secretary

Amicus Brief

MOTION FILED
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81-1002

IN THE

Supreme Court of the United States

October Term, 1981

THE CLEVELAND ELECTRIC ILLUMINATING COMPANY,
Appellant,

v.

OFFICE OF CONSUMERS' COUNSEL, SENIOR CITIZENS COALITION, GREATER CLEVELAND WELFARE RIGHTS ORGANIZATION, INC., WESTERN RESERVE ALLIANCE, NORTH SHORE ALERT, CLEVELAND CHAPTER OF OHIOANS FOR UTILITY REFORM,

and

THE PUBLIC UTILITIES COMMISSION OF OHIO,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF OHIO

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF *AMICUS CURIAE* OF EDISON ELECTRIC INSTITUTE IN SUPPORT OF APPELLANT

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December 23, 1981

QUESTION PRESENTED:

Does a State statute which (as construed by the State Supreme Court) requires that utility rates be determined on the basis of a rigid formula that prohibits recovery of costs prudently incurred by the utility in discharge of its express obligations under the same statute violate the Fifth and Fourteenth Amendments to the United States Constitution?

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Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF OHIO

MOTION OF EDISON ELECTRIC INSTITUTE FOR LEAVE TO FILE BRIEF *AMICUS CURIAE*

Edison Electric Institute hereby respectfully moves for leave to file the attached brief *amicus curiae* in this case. The consents of appellant and of appellees Public Utilities Commission of Ohio and the Office of Consumers' Counsel have been obtained. The consents of the remaining appellees were requested but refused.

The interest of Edison Electric Institute in this case arises from the fact that it is the national association of investor-owned electric utility companies in the United States. Its members serve 99.1 percent of all customers of the investor-owned segment of the industry and 77.1 percent of the nation's electricity users.

In the instant case in the Supreme Court of Ohio, appellee Office of Consumers' Counsel, argued that the question here involved arises solely as a result of the uniqueness of Ohio law. Notwithstanding this representation to the Ohio Supreme Court, within less than a month after that Court's ruling, the Office of Consumers' Counsel characterized it as a "landmark decision which establishes a national precedent." The issue raised by the decision of the Ohio Supreme Court is not one involving the construction of that statute. Rather it is whether, assuming the correctness of that construction, such a statute is repugnant to the United States Constitution. It is believed that the brief which *amicus curiae* is requesting permission to file contains an exposition of the National significance and importance of the resolution of the matter before the Court, which Edison Electric Institute is specially qualified to present.

Respectfully submitted,

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TABLE OF CONTENTS

	PAGE
QUESTION PRESENTED	(i)
TABLE OF AUTHORITIES	(iii)
INTEREST OF AMICUS CURIAE	1
CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED	5
SUMMARY OF ARGUMENT	6
ARGUMENT	8
A. The Ohio statute, as construed by the Ohio Supreme Court, represents a return to ratemakng by rigid legislative formula which ignores the teachings of this Court	8
B. The Ohio statute, as construed by the Ohio Supreme Court, is arbitrary and irrational	10
C. This Court's historic role and the national interest warrant review by this Court	11
CONCLUSION	13

TABLE OF AUTHORITIES

	PAGE
UNITED STATES CONSTITUTION	
AMENDMENT V	7,8
AMENDMENT XIV	7,8
Cases:	
Chicago, Burlington and Quincy Railroad Co. v. *Chicago*, 166 U.S. 226 (1897)	8
Covington & Lexington Turnpike Road Co. v. *Sandford*, 164 U.S. 578 (1896)	2,8,10,11
Federal Power Commission v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944)	7,9,11,12
Federal Power Commission v. *Memphis Light, Gas and Water Division*, 411 U.S. 458 (1973)	7,9,11,12,13
Federal Power Commission v. *Natural Gas Pipeline Co.*, 315 U.S. 575 (1942)	9,11
Ferguson v. *Skrupa*, 372 U.S. 726 (1963)	10,12
Missouri ex rel. Southwestern Bell Telephone Co. v. *Public Service Commission*, 262 U.S. 276 (1923)	11
NEPCO Municipal Rate Comm. et al v. *Federal Energy Regulatory Commission*, ___ F. 2d ___ (October 15, 1981)	3
Pacific Gas & Electric Co. v. *City of San Francisco*, 265 U.S. 403 (1924)	11
Permian Basin Area Rate Cases, 390 U.S. 747 (1968)	8,9,10,12
Smyth v. *Ames*, 169 U.S. 466 (1898)	2,11
Stone v. *Farmers' Loan & Trust Co.*, 116 U.S. 307 (1886)	8,10
UGI Corp. v. *Pennsylvania Public Utility Commission*, 49 Pa. Commw. Ct. 69, 410 A. 2d 923 (1980)	3
Webb's Fabulous Pharmacies, Inc. v. *Beckwith*, 449 U.S. 155 (1980)	8

PAGE

Statutes:

Ohio Revised Code, Sections 4905.22, 4905.37, 4909.15 2,10

Miscellaneous:

Cicchetti and Shaughnessy, Our Nation's Gas and Electric Utilities: Time to Decide, 108 Pub. Util. Fort. No. 12, 29 (December 3, 1981) 5

Kahn, "Utility Regulation Revisited", Address to, New England Conference of Public Utilities Commissioners Annual Symposium, Dixville North, New Hampshire, June 15, 1981 3

Edwards, Address to United States National Committee of the World Energy Conference and Edison Electric Institute, New York, New York, October 28, 1981 4

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ON APPEAL FROM THE SUPREME COURT OF THE STATE OF OHIO

BRIEF *AMICUS CURIAE* OF EDISON ELECTRIC INSTITUTE IN SUPPORT OF APPELLANT

Edison Electric Institute ("EEI") hereby submits its brief *amicus curiae* in support of the appeal filed by Cleveland Electric Illuminating Company ("CEI").[1]

INTEREST OF AMICUS CURIAE

EEI is the national association of investor-owned electric utility companies in the United States. Its members serve

1. EEI has obtained the written consents of appellant, and appellees Public Utilities Commission of Ohio and Office of Consumers' Counsel, to the filing of this brief, and such written consents have been filed with the Clerk of this Court. Because the written consents of the other appellees, which were requested, have been refused, EEI by motion, is requesting this Court to permit this filing.

99.1 percent of all customers of the investor-owned segment of the industry and 77.1 percent of the nation's electricity users. The Ohio Supreme Court has held that the Ohio public utility law (Ohio Revised Code, Title 49) and particularly Chapter 4909 of that Title governing the determination of rates by the Ohio Public Utilities Commission (the "Ohio Commission") precludes any recovery through rates of costs of planning and preliminary engineering prudently incurred by CEI in carrying out its obligation under another Chapter of that same Title to provide necessary and adequate facilities, when the projects for which such costs were incurred were prudently canceled by reason of changed circumstances. As so construed by the Ohio Supreme Court, the Ohio statute resurrects the pre-20th century practice of direct legislative determination of allowable utility rates by specific tariffs or specific formulae that ignored the Constitutional constraints upon such governmental actions. [2] The grave constitutional issue so presented was not even addressed by the Ohio Supreme Court.

The Ohio Office of Consumers' Counsel ("Consumers' Counsel") had represented to the Ohio Supreme Court that the Ohio ratemaking statute is "uniquely specific"[3] and that that court should disregard the decisions of the Federal Energy Regulatory Commission (and its predecessor Federal Power Commission) and of the eighteen State utility commissions that had previously decided this issue, as had the Ohio Commission, by fixing rates that made provision for the amortization of such costs. The Supreme Court recognized that "the overwhelming weight of authority"

2. *Smyth v. Ames*, 169 U.S. 466 (1898), involved, for example, a Nebraska statute prescribing classifications of freight and rates for intrastate railroad transport. Similarly, *Covington & Lexington Turnpike Road Co.* v. *Sandford*, 164 U.S. 578 (1896) involved a Kentucky statute's prohibiting a turnpike company from charging tolls in excess of the rates specified therein.

3. Notwithstanding its representation to the Ohio Supreme Court that the Ohio statute is "uniquely specific", within less than a month after that Court's ruling, Consumers' Counsel characterized it as a "landmark decision which establishes a national precedent."

from other jurisdictions supported the Ohio Commission's decision[4], but stated that no other case had considered the propriety of the Ohio Commission's amortization allowance with reference to Ohio law, and then held that the Ohio statute does not permit recognition of such costs in fixing rates.

There is wide-spread recognition that regulation of the rates of electric utilities is not working throughout the nation and that there is a substantial likelihood that electric utilities will be unable to attract the capital needed to build the facilities to light, heat and cool the nation's homes, power its factories and meet the requirements of its commercial establishments.[5] Since 1973, the average electric utility common stock has been selling well below nominal dollar book value (*e.g.*, 75% of nominal book value in

4. In *UGI Corp.* v. *Pa. Pub. Util. Comm'n*, 49 Pa. Commonw. Ct. 69, 86-88, 410 A. 2d 923, 932-933 (1980), the court reversed a utility commission order for failure to permit recovery through rates of similar costs and directed the commission to allow amortization of such costs as an operating expense. Moreover, subsequent to the Ohio Supreme Court's decision, the United States Court of Appeals for the District of Columbia upheld a rate order of the Federal Energy Regulatory Commission that allowed for ratemaking purposes amortization of similar costs, stating that:

> "[b]ecause it would be inequitable to place on the utility the entire loss of expenditures prudent when made, FERC allowed recovery thereof over time." *NEPCO Municipal Rate Committee et al.* v. *Federal Energy Regulatory Commission*, ___ F. 2nd ___ (October 15, 1981)

5. See, *e.g.*, the paper "Utility Regulation Revisited" by Professor Alfred E. Kahn, former Chairman of the Public Service Commission of New York and of the Civil Aeronautics Board, and author of a leading text on public utility economics and regulation, presented at the Annual Symposium of the New England Public Utility Commissioners on June 15, 1981, in which he characterized, at 1, the financial condition of electric utilities as "abysmal" and stated that their deteriorated financial performance "represents also a profound failure—I am tempted even to characterize it as a crisis—of the institution of regulation itself." In a speech delivered on October 28, 1981 before the United States National Committee of the World Energy Conference, United States Secretary of Energy James B. Edwards characterized the electric utility industry as in a "financial morass", and stated at 2:

[footnote continued on following page]

1980 and even less today) and, in terms of monetary units of equivalent purchasing power, at only a small fraction of the sums invested.

Since the Federal Energy Regulatory Commission regulates on average less than 10% of the revenues of investor-owned electric utilities, the institutional failure of rate regulation of electric utilities is predominantly a failure of State, rather than Federal, regulation. Federal officials have, from time to time, sought to persuade State ratemaking agencies to recognize the public need for rate regulation that is not confiscatory in result,[6] but there has been little response by State ratemaking bodies and legislatures.

In a recent article, the former Chairman of the Wisconsin Public Service Commission has put the problem bluntly:

> "Our nation's gas and electric utilities are in financial difficulty. Political pressure is still being brought to bear on them. Without a dramatic reversal it is safe to conclude that matters will get far worse. The ultimate losers are: (1) those consumers that pay prices that could be lowered; (2) taxpayers that must pay more as industry emigrates to other

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"We must act now lest we find the President's Economic Recovery Program derailed because of deteriorating electric service. There is no doubt at all in my mind that unless the utilities are able to finance construction of new plants, our Nation's productivity will be jeopardized. We will face periodic brownouts, load cycling and other interruptions that will force factories to curtail their operations and seriously inconvenience the public. Furthermore, utilities will be forced to continue their uneconomic use of oil unless they have the money to build new plants."

6. In his October 28, 1981 speech, *supra* Note 5, United States Secretary of Energy James B. Edwards stated:

> "We have to convince state public service commissions and the Federal Energy Regulatory Commissions that utilities deserve a realized rate of return at least 4 percentage points higher than the effective rate now, which hovers below about 12 percent. When a utility has to pay 19 percent on its bonds, it can't continue in business indefinitely if it's earning far less than that."

countries; and (3) people seeking work in a contracting economy. In short, we all lose if we continue down this path."[7]

The institutional failure of the regulation of electric utility rates is, in part, the consequence of the actions of rate regulatory bodies who frequently find it too difficult to face the issues and make the factual, legal and policy determinations necessary to carry out the earlier teachings of this Court. It is also, in part, the consequence of the actions and inactions of State legislative bodies that find it difficult to give adequate consideration to the long-run needs of electric utilities if they involve near-term increases in electric charges. But it is also, in significant measure, the consequence of a perception—which EEI hopes is unfounded—by State agencies and legislatures that this Court is unwilling to make clear for the current generation that legislatures and rate regulatory bodies may not, in the guise of regulation, appropriate investor-supplied capital.

EEI assumes that Consumers' Counsel was correct in representing to the Ohio Supreme Court that the Ohio statute is "uniquely specific". If so, as CEI advised that court, that statute is also "uniquely unconstitutional."

In urging that the Court note probable jurisdiction of CEI's appeal, EEI is representing not only the interests of its members and of the millions of investors in EEI's member companies; it is also representing the long run interests of the millions of customers served by EEI's members and, indeed, the national interest, in safe, adequate and reliable electric service.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The pertinent provisions of the Fifth and Fourteenth Amendments to the U. S. Constitution and of the Ohio

7. Cicchetti and Shaughnessy, "Our Nation's Gas and Electric Utilities: Time to Decide", 108 Pub. Util. Fort. No. 12, 29 (December 3, 1981).

Revised Code are reprinted in the CEI Jurisdictional Statement.

SUMMARY OF ARGUMENT

During the period 1973 - 1980, CEI expended approximately $56 million on planning, preliminary engineering, site surveys, environmental, geological and seismic studies, licensing permits and other regulatory authorizations work on four proposed nuclear generating units. The applicable rules and regulations of the Ohio Commission required that such expenditures be capitalized at the time of expenditure. If the units had been completed and placed in service, such expenditures would have been recovered as part of the allowable depreciation charges over the units' service lives. In 1980, CEI determined, in the light of changed conditions, that the four units should not be constructed. In fixing CEI's rates in 1980, the Ohio Commission, finding that CEI's "decisions were reasonable and prudent at every step of this process", made provision for recovery of such expenditures by the allowance of amortization of such expenditures over a 10-year period.

It is unquestioned that the Ohio statutory ratemaking requirements in effect during the period of the expenditure of the funds precluded recognition of such expenditures in operating expenses or in rate base at the time of expenditure. It is also unquestioned that the return allowance authorized by the Commission during this period made no provision for the potential risk that CEI would not be permitted to recover such expenditures in some manner through rates charged by CEI to its customers if the projects were abandoned before completion.[8]

8. On remand from the Ohio Supreme Court, the Ohio Commission directed CEI to reduce its then existing rates by an amount equal to the revenue requirements attributable to the amortization previously authorized by the Commission. In so doing, it made no provision for adjustment of the allowed rate of return to give recognition to this risk.

Upon appeal by Consumers' Counsel, the Ohio Supreme Court held that the Commission exceeded its statutory authority in allowing amortization of such expenditures. As construed by the Ohio Supreme Court, the Ohio statute limits the Ohio Commission, in fixing "just and reasonable rates" to consideration of "the normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period" and, aside from minor adjustments, does not permit the consideration of other factors.

Thus, the issue here presented is not whether a rate regulatory agency has properly exercised its discretion in balancing consumer and investor interests, as required by *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) and *Federal Power Commission* v. *Memphis Light, Gas and Water Division*, 411 U.S. 458 (1973). Although not stated in those terms, the Ohio Commission clearly concluded that the rates that it had fixed (which included provision for the amortization of the subject costs) did appropriately balance consumer and investor interests. But the Ohio statute, as construed by the Ohio Supreme Court, does not permit such a balancing. Instead, it precludes the recovery through rates of prudent expenditures, thereby causing investors to incur substantial losses for which they have not been and will not be compensated. Having so construed that statute, the Ohio Supreme Court should have held the statute invalid as repugnant to the Fifth and Fourteenth Amendments because, in the guise of regulation, it requires the taking of private property for public use without just compensation. In so doing, it does not bear a rational relationship to a Constitutionally permissible objective.

ARGUMENT

A. THE OHIO STATUTE, AS CONSTRUED BY THE OHIO SUPREME COURT, REPRESENTS A RETURN TO RATEMAKING BY RIGID LEGISLATIVE FORMULA WHICH IGNORES THE TEACHINGS OF THIS COURT.

The Fifth Amendment prohibits the taking of private property for public use without just compensation. For more than 80 years, this Court has held (and recently reaffirmed) that this prohibition of the Fifth Amendment applies against the States through the Fourteenth Amendment. *Chicago, Burlington and Quincy Railroad Co.* v. *Chicago*, 166 U.S. 226, 239 (1897). In *Webb's Fabulous Pharmacies, Inc.* v. *Beckwith*, 449 U.S. 155 (1980), this Court said, at 164:

> "To put it another way: a State, by *ipse dixit*, may not transform private property into public property without compensation . . . This is the very kind of thing that the Taking Clause of the Fifth Amendment was meant to prevent. That Clause stands as a shield against the arbitrary use of governmental power."

While the Fifth and Fourteenth Amendments do not, of course, forbid the States from regulating the conduct and rates of public utilities, as the Court observed in *Permian Basin Area Rate Cases*, 390 U.S. 747, 769 (1968):

> "It is, however, plain that the 'power to regulate is not the power to destroy', *Stone* v. *Farmers' Loan & Trust Company*, 116 U.S. 307, 331; *Covington & Lexington Turnpike Co.* v. *Sandford, supra*; and that maximum rates must be calculated for a regulated class in conformity with pertinent constitutional limitations."[9]

9. Both the *Stone* and *Covington & Lexington* cases involved the applicability of the Fifth and Fourteenth Amendments to rate regulation.

At least since *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U.S. 575 (1942), this Court has emphasized that the Constitution does not require the use of any particular method or formula in the determination of utility rates. Rather, in *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U.S. 591 (1944), it held that the "just and reasonable" rate standard of the Natural Gas Act requires the balancing of consumer and investor interests so that, on the one hand, consumers are protected against exploitation and, on the other, the utility is permitted "enough revenue not only for operating expenses but also for the capital costs of the business" to provide a return "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." *Hope*, *ibid*, at 603; *Federal Power Commission* v. *Memphis Light, Gas and Water Division*, 411 U.S. 458, 466 (1973). And, in *Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968), this Court held that "the just and reasonable standard of the Natural Gas Act 'coincides' with the applicable constitutional standards."

In reaching its decision to fix rates that made provision for the amortization of CEI's expenditures for planning and preliminary engineering, the Ohio Commission found that such expenditures had been incurred on behalf of CEI's customers to assure that adequate service would be provided, that they had been prudent every step of the way, and that rejection of the amortization would have a very direct impact on CEI's financial performance as, in the absence of the funding of the amortization through rates, CEI would be required to write off these costs currently. Its ultimate view was:

> "Thus, we now see the wisdom of the standard emerging from the cases from other jurisdictions; if the expenditures are prudent, amortization should be permitted."

The Ohio Supreme Court rejected that view, even though it recognized that "the overwhelming weight of authority from other jurisdictions supports the position of the commission." That Court treated the issue as solely one of construction of the Ohio statute and it refused to consider the constraints on State ratemaking legislation imposed by the Constitution.

B. THE OHIO STATUTE, AS CONSTRUED BY THE OHIO SUPREME COURT, IS ARBITRARY AND IRRATIONAL.

Chapter 4905 of Title 49 of the Ohio Revised Code expressly requires utilities to furnish necessary and adequate facilities.[10] To meet that requirement, CEI had to make expenditures of the nature here involved. The Commission found that the 1973 decision to initiate such expenditures was reasonable and based on the best data available, and that such expenditures had been prudent every step of the way. Yet, Chapter 4909[11] of Title 49 of the Ohio Revised Code (as construed by the Ohio Supreme Court) prohibits the Commission from establishing rates that permit recovery of such expenditures.

EEI recognizes fully the limits on the Court's review of State statutes reflected in *Ferguson v. Skrupa*, 372 U.S. 726, 730-732 (1963). But, in *Ferguson*, the Court also recognized that State statutes can run afoul of a specific Federal constitutional requirement and, thereby, be invalid. The Fifth and Fourteenth Amendments are just such a specific Federal constitutional limitation on State legislative action.[12]

10. See Section 4905.22. Moreover, Section 4905.37 of that Chapter authorizes the Commission to prescribe by order the installation of facilities, upon its own motion or upon complaint, if it finds that the equipment is inadequate.

11. The Ohio Court's particular focus was on Section 4909.15 of that Chapter.

12. As previously noted, in *Permian Basin*, *supra*, at 769-770, the Court recognized once again that the Fifth and Fourteenth Amendments place some limits on State exercise of ratemaking authority, citing *Stone* v. *Farmers' Loan & Trust Co.*, 116 U.S. 307, 331 (1886) and *Covington &*

The Ohio public utility law, by commanding on the one hand that an electric utility expend funds for planning and preliminary engineering to discharge its public utility responsibilities, but, on the other, denying recovery of prudent expenditures for such purposes, is arbitrary and irrational — *i.e.*, it does not bear a rational relationship to a constitutionally permissible objective.

C. THIS COURT'S HISTORIC ROLE AND THE NATIONAL INTEREST WARRANT REVIEW BY THIS COURT.

During the period between *Smyth* v. *Ames*, *supra* (1898) and *Natural Gas Pipeline Co.*, *supra* (1942), the Court heard an unduly large number of rate cases, as it sought to clarify the so-called "rule of *Smyth v. Ames*". Justices Brandeis and Holmes were highly critical of these efforts. See, *e.g.*, *Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service Commission*, 262 U.S. 276, 289 (1923), (cited approvingly in *Hope*, *supra*, at 603) and *Pacific Gas & Electric Company* v. *City of San Francisco*, 265 U.S. 403, 416 (1924). Yet, they also recognized that investors in public utility securities are constitutionally entitled to a return of, and on,[13] the capital they supplied, so long as the resulting rates are not prohibitive, exorbitant or unduly burdensome to the public. *Southwestern Bell*, *supra*, at 290; *Pacific Gas*, *supra* at 425.

Since *Natural Gas Pipeline* and *Hope*, EEI believes that State ratemaking actions have become unhealthily insulated from review by the Court. It is one thing for the Court, quoting Justice Douglas (who was the author of the Court's opinions in both *Hope* and *Memphis Light*), to refuse

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Lexington Turnpike Co. v. *Sandford*, 164 U.S., 578, 593 (1896), and that a balancing of consumer and investor interests in accordance with *Hope* criteria is necessary to pass Constitutional muster.

13. CEI's request was much more modest. It sought only the return of its prudent investment by amortization over a 10-year period without any return on the unamortized balance.

to sit as a superlegislature to weigh the wisdom of legislation. *Ferguson, supra* at 731. It is another for the Court to refuse to consider, year after year, the application of Constitutional criteria to ratemaking actions of State agencies, courts and (as here) legislatures. The Court determined in *Hope* and *Memphis* that ratemaking agencies are charged with balancing consumer and investor interests. No such balancing was even hinted at by the Ohio Supreme Court in construing the Ohio statute as prescribing severe constraints on the exercise of discretion by the Ohio Commission. This is not a case in which the issue is whether a regulatory agency exercised its discretion to produce a constitutionally acceptable result. Rather it presents the blunt question of whether a statute that mandates nonrecovery *in any manner* of $56 million of prudent expenditures made in accordance with the requirements of other provisions of the same statute is in irreconcilable conflict with express requirements of the Constitution.

EEI believes that the Court is similarly charged with balancing the flexibility accorded the States and their agencies in developing ratemaking methods and formulae with some evaluation by the Court of the end result of such actions in the light of Constitutional limitations. If the Court invariably refuses to consider rate case appeals brought to it from the States, the Constitutional rights of investors acknowledged by the Court in *Hope*, *Memphis Light* and *Permian Basin* are likely to be ephemeral.

The Ohio Supreme Court is charged not only with the construction of Ohio law. It is also charged with the application of the Federal Constitution to such laws. As previously noted, in this case, it refused to even address the Constitutional issues presented to it. As the Court stated, at 474, in *Memphis Light* (in which the public utility involved was a gas pipeline):

> "We note in closing, however, that the judgment of the Court of Appeals is reversed *in toto*. Its holding

> that the consumer interests were not furthered by the Commission's action is short of the application of the appropriate standard for review. As already noted, under *Hope Natural Gas* rates are 'just and reasonable' only if consumer interests are protected and if the financial health of the pipeline in our economic system remains strong."

Review by this Court is warranted to assure that the Ohio Court and other State courts do not ignore their dual responsibilities.

CONCLUSION

As pointed out by Secretary Edwards, the National interest in restoration of the financial health of the electric utility industry can hardly be overstated. Such restoration can only be achieved through renewed recognition that investors have Constitutionally protected rights that the electric utilities in which they have invested be allowed to charge rates that, so long as they do not exploit consumers, preserve the utilities' financial integrity.[14]

The holding of the Ohio Supreme Court that the Ohio Commission could not permit CEI to recover concededly prudent expenditures because the Ohio statute did not make provision for such recovery did not apply the appropriate standard of review because — just as was the case in the decision of the Court of Appeals in *Memphis Light* — it failed to balance the interests of consumers and investors. Having so construed the Ohio public utility law, the Ohio Court should have held that law invalid as repugnant to

14. The Ohio Commission, of course, did not find the rates it set exploitative of consumers. The Ohio Court did not address the issue.

the United States Constitution. Because it failed to do so, correction by this Court is required.

Respectfully submitted,

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Dated: December 23, 1981

CERTIFICATE OF SERVICE

I hereby certify that on the 23rd day of December, 1981, copies of the foregoing Motion for Leave to File Brief Amicus Curiae and Brief Amicus Curiae were mailed, by first class mail, postage prepaid, to The Cleveland Electric Illuminating Company, Attention: Alan P. Buchmann, Squire, Sanders & Dempsey, 1800 Union Commerce Building, Cleveland, Ohio 44115, Office of Consumers' Counsel, Attention: Gary M. Petroff, 127 East State Street, Columbus, Ohio 43215, Senior Citizens Coalition, Greater Cleveland Welfare Rights Organization, Inc., Western Reserve Alliance, North Shore Alert and Cleveland Chapter of Ohioans for Utility Reform, Attention: Joseph P. Meissner, Cleveland Legal Aid Society, 1223 West 6th Street, Cleveland, Ohio 44113 and The Public Utilities Commission of Ohio, Attention: Marvin I. Resnik, Public Utilities Section, 375 South High Street, Columbus, Ohio 43215. I further certify that all parties required to be served have been served.

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